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RETAIL MANAGEMENT

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RETAIL MANAGEMENT
SECOND YEAR

PAPER - III

RETAIL BUYING AND MERCHANDISING

UNIT 1-10

MADURAI KAMARAJ UNIVERSITY,
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Paper IV – RETAIL BUYING AND MERCHANDISING_2637

UNIT I

Planning Merchandise Assortments-Organizing the buying process by categories-category management- the buying Organization

UNIT II

Setting the financial objectives for the merchandise plan-Gross margin return on inventory management (GMROI)-Measuring inventory turnover-Sales forecasting.

UNIT III

Assortment planning process - Variety - Assortment-Product management.

UNIT IV

Trade offs between variety, Assortment and Product Availability-Assortment plan-Product mix trends

UNIT V

Buying systems for Staple Merchandise- Buying systems for Fashion Merchandise.

UNIT VI

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UNIT IX

Merchandise pricing-Setting the retail price-Pricing objectives-Pricing strategies-Pricing methods-Pricing adjustments-Price discrimination.

UNIT X

Retail Communication- Role of communication in retailing-Methods of communication-Planning the retail communication programs-Implementing and Evaluating the retail communication programs.

SUGGESTED READINGS

1. Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.
2. Retail Management- ICFAI Center for management Research publications.
3. Merchandise buying and management-John Donnellan, Fairchild publications.
4. Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985.

UNIT I

Structure:

1.0 Introduction
1.1 Unit Objectives
1.2 Concept of Retailing
1.3 The Changing Pyramid of Retailing
1.4 Retail Merchandising: The Major Function of Retailing
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1.0 Introduction

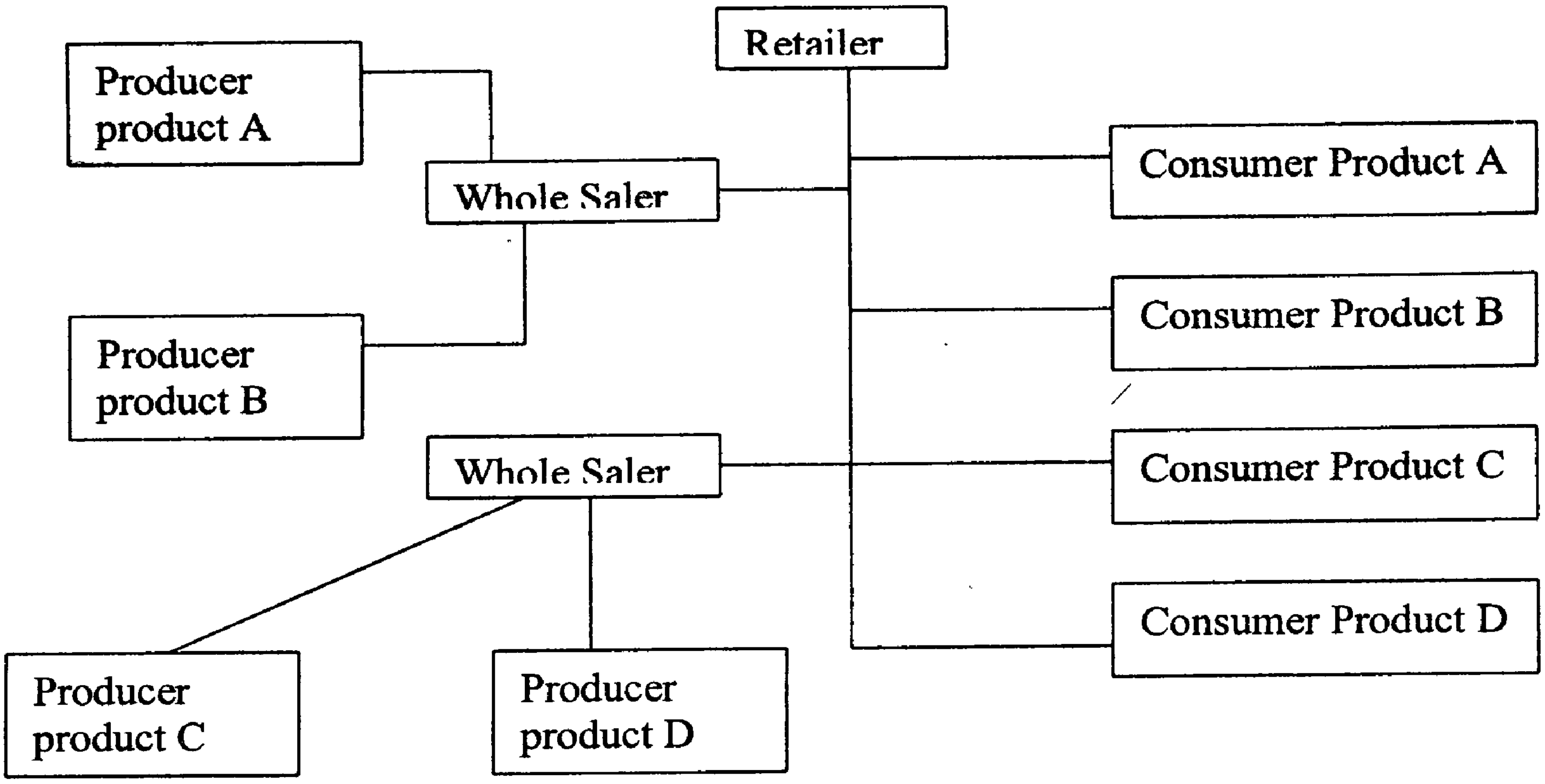
'Retailer' the French word provides the origin for the word 'Retail' which means to break a bulk. Retailers are the one who stands in direct contact with the consumers, is typically the last rung at any distribution channel. World over retailers aims at attaching a wide fund of customers to their place by focusing on product quality, prices and customer services. Strategically they achieve their objective commonly by increasing the width of their assortments.

For the ultimate objective of attaching customers retailers adds goods and services that may be unrelated to each other and design an portfolio of products which will increase their over all revenue, drive consumers for impulsive buying, high stock turn over due to fast selling of goods and services, attract varying target market, provides one stop shopping and reduces the impact of seasonality and competition.

1.1Unit Objectives:

- Understanding Retail Management and Merchandising Process
- Understanding Organizing of Buying Process by Category and Category Management.
- Learning the Structure of Buying Organisation.

1.2 Concept of Retailing:



The above diagram shows clearly the concept of retailing, with the increasing competition manufactures crowd the retailers for selling their products. The retail pyramid is also project an inverse figure where customers also crowd retailers for shopping, in this situation with wide array of products as well as buying habits of consumers changing retailers are in a position to cash in on the opportunity.

1.3 The changing pyramid of retailing

Even retailers are in a position of advantage, consumer are also highly informed and aware and their tastes, preferences are dynamic. In such situation retail organizations rely on proper merchandising and ensuring optimal merchandise mix which will consistently attract consumers towards the retail organization

1.4 Retail Merchandising: The major function of retail organization

Merchandising is a process of inventory planning and management in retail organization. Profitability of any organization, rely on proper merchandising. The following functions , of typical retail organization clearly emphasis the contribution of merchandising to the process of any retail organization.

1) **Buying merchandise**
2) **Shipping merchandise**
3) **Receiving and checking incoming shipment**
4) **Setting prices**
5) **Inventory storage and control**
6) **Proper window displays**
7) Keeping store ambiance
8) **Customer research to enhance information**
9) **Communication through advertisement, personal selling etc.,**
10) Facilitating shopping through proper site and short check out
11) **Personal management**
12) **Repairs and alteration of merchandise**
13) Billing and handling receipts and financial records
14) Credit operations
15) **Gift wrapping and delivery**
16) **Returning unsold or damaged merchandise to vendor**
17) **Sales forecasting and budgeting**
18) Coordination of all the above activities

1.5 Merchandise Management

The primary goal of most retailers is to sell merchandise and service. Nothing is more central to the strategic thrust of the retailing firm. Thus deciding what to buy and how much is a vital task for any retailer.

Merchandise management is a process by which the retailer accepts to offers the 7^{Rs} of merchandising

1) the right product
2) the right place
3) the right quantity
4) the right quality
5) the right price
6) the right mix or assortment
7) the right time

It comprises of analyzing, planning, acquiring, handling and controlling the merchandise investment in an retail operation

1.6 Growth of Merchandising Function

Initially the number of retail stores and its size is comparatively small,hence the function of buying the merchandise, pricing and communicating etc where much simpler.

When the size and number expands the buyer alone find it difficult to merchandise based on sales volume, hence a planner came into existence to bridge the gap between stores and buyer who provides significant information from store level and buyer execute their job based on the insights derived from the planner. This function is termed as merchandising which aims at providing the right mix which the target group prefers.

1.7 Factors affecting merchandise function

There are several function which affect the merchandise function They are:

1) Size of the organization

Size of the organization affect merchandising because no two stores are organized the same way, an individual retailers process of merchandising will vary from that of an merchandising function of chain stores

2) Merchandise to be carried

It influences the function of buying. Buying for staples is different from fashion goods. Demand, supply patterns and life cycles trends for these products vary heavily.

3) Organization structure

Departmentalization, authority and responsibility structures vary from organization to organization. Some organizations appoint buyer and merchandiser separately where as another appoint a single person to carry out both the job.

4) The type of the store

1.8 Merchandise Hierarchy

A clear definition of merchandise hierarchy is must for planning merchandise mix for a retail organization. It is the activity of grouping the merchandise mix at different levels from the Top most classification to stock keeping unit (SKO)

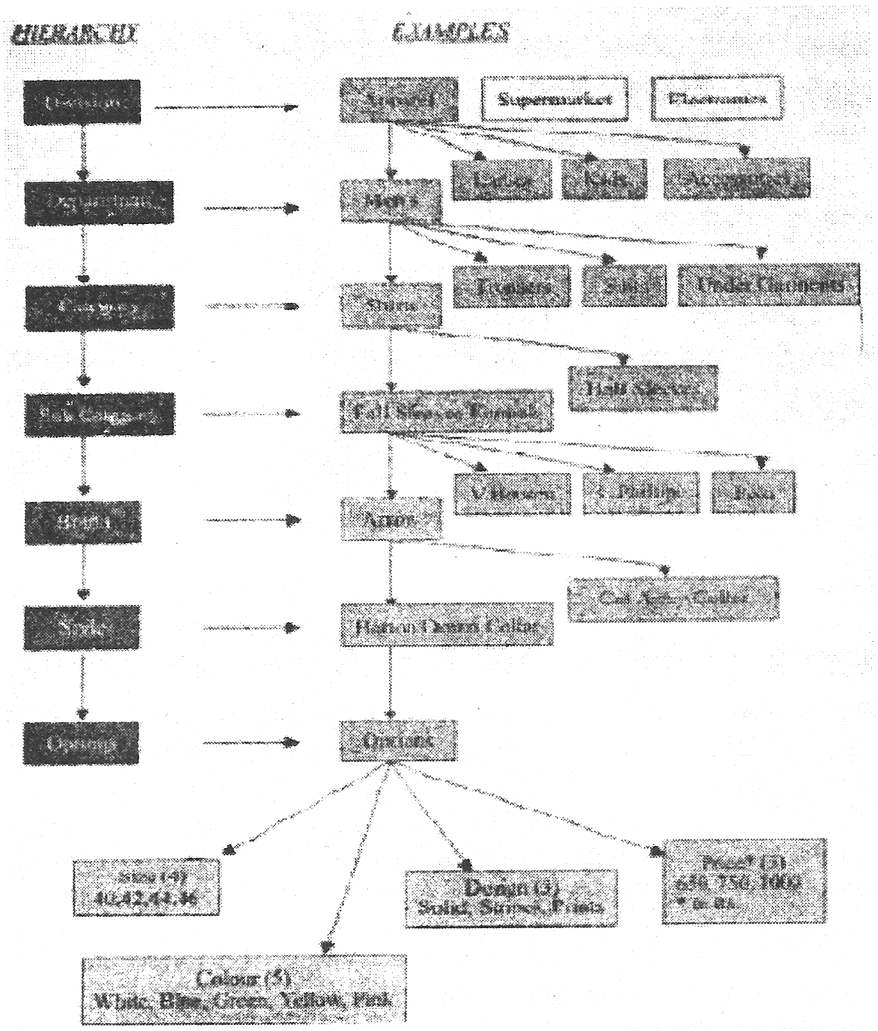


Diagram Showing Merchandising Hierarchy

Above diagram Cleary defines the merchandise hierarchy for the apparel division of an retail organization this would aid in devising the ratios of each categories to be carried by the retail organization according to it customer insight which provide a base for arriving at the optimum merchandise mix

1.9 Process of merchandise management

Organize the buying process by category

↓

Set financial objectives for merchandise

↓

Develop assortment plan

↓

Buying staple Fashion goods

↓

Open to buy systems

↓

Allocate merchandise to stores

↓

Handling merchandise

↓

Analyze merchandise performance

↓

Branding merchandise

↓

Merchandise pricing

↓

Communicating merchandise

Merchandise management process commonly follows the above mentioned sequence. It includes the physical purchase of products and services and how those products and services are brought to the retail outlet, handled and finally placed for sale. When merchandise decisions are inconsistent with strategy it can damage the retailers image and confuse customers. Hence merchandise management process should complement the strategic focus of the respective organization

1.10 Merchandising planning

Profit is the aim of any business, retailing is no exception, the function of planning of the merchandise is the major part of retail organization this involves planning and analyzing.

Analysis is the starting point of merchandise planning this includes understanding the consumer needs and wants, their buying process, insight about what product is actually selling and where the demand is. External sources of information like surveys, magazine, trade publications and associations are also to be consulted. Information thus gathered needs to be analyzed, which will form the basis of sales forecast, which is the first step of merchandise planning. Planning of merchandise buying, receiving and recording the receipt and distributing it to the stores is also of great importance in merchandise management.

Step 1: Forecasting sales

Forecasting is predicting of what consumers may do under a given set of condition. It may be made by a merchandiser, or by the top management depending on the retail organization.

It answers the questions like:

How much to purchase?

Which product is to be purchased?

What is the assortment plan?

What price is to be fixed?

What is merchandise mix?

Step 2: Defining the merchandise requirements

Defining the merchandise requirements follows the sales forecasts, which aims at arriving at the inventory level for each product category and also arriving at the financial requirement to execute the merchandise which is called the merchandise budget. There are several techniques to arrive at the merchandise budget and inventory levels which we will discuss later.

Step 3 Controlling merchandise

Merchandise controlling is a process of limiting over buying and under buying, preventing the loss of sale due to stock out, purchasing with the budgeted limits and reduce mark downs, which may arise because of excess buying. Open-to-buy system is a technique used to achieve those objectives which will be discussed elaborately later.

Step 4: Planning Assortment

Assortment planning involves the determination of the quantities of each product that we will purchase so as to fit into the overall merchandise plan. Details of the size, color, materials, brands etc have to be specified. The main purpose of creating assortment plan is to create a balanced assortment of merchandise to match the customer needs.

1.11 Organizing of the buying process by category

In general a category is an assortment of items that the customer sees as reasonable substitutes for each other. Retailers and their vendors might begin with different definitions of a category. A vendor might assign shampoos and conditioners to different category based on the differences in product attributes where as other may assign them to same category treating them as hair care products. No matter how the category is defined, supply chain members must agree on the category definition, and it must be based on what is logical to the consumer.

Category Management

Category management is the process of managing a retail business with the objective of maximizing the sales and profit of a category. An important reason for adopting category management is that one person is ultimately responsible for the success or failure of a category. And it is easier to manage to maximize profits if specialized category managers are assigned.

The category captain

Some retailer's turn to one favored vendor to help them manage a particular category knows as the category captain. This supplier forms an alliance with a retailer to help gain customer insight, satisfy customer needs and improve the performance and profit potential across the entire category.

A potential problem with establishing a category captain, is that they could take advantage of their position. Hence retailers should not turn over important decisions to the vendors (ie) the category captain. Working with them and carefully evaluating their suggestions is a much more prudent approach.

1.12 Components of Category Management

There are six components to category management, two factors are considered essential for the functioning of category management which is linked to the company's overall mission and goals: they are the strategy and Business processes other things follows are performance measurement, trading partner relationship, organizational capability and information technology.

Category management process

A category is a merchandise group that addresses similar consumer needs and wants. Goods in a category are displayed and sold together in a retail environment so that customer choices are easier, thus enhancing the shopping experience.

Category management is similar to brand management, as product groups become the focal point in terms of development, merchandising and marketing .The category management process in retailing involves the following steps

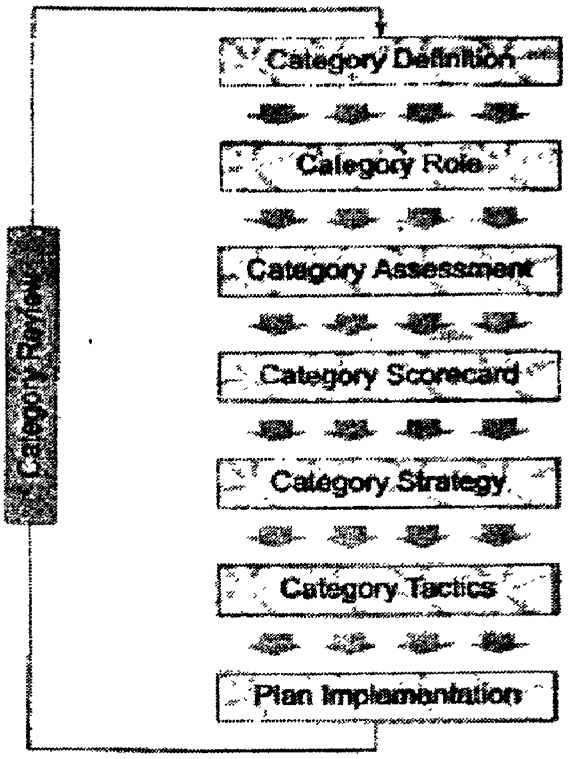


Diagram Showing Category Management Process

Category Vision –

Top managements view of what each category ought to achieve in terms of customer satisfaction value and differentiation.

Category definition-

A category definition should be based on how the customers buys and not on how the retailer buys.

Category role

Defines the priority and the importance of the various categories in the over all business. Normally four categories exist

- Destination category- the main product offering
- Routine / Preferred category –consumers buy as a route habit
- Occasional /Seasonal category – which bought when available and needed.
- Convenience category- consumer finds convenient to buy at the neighborhood retail shop

Category assessment-

Assessing the performance of the category with respect to Turnover, Profit ,ROA etc. It also include assessment of consumers ,the market, the retailer and the supplier.

Category scorecard-

Acts as an yardstick to measure the performance based on targets of sales margins and Gross margins return on investment(GMROI)

Category strategy-

Developing strategies that capitalize on category opportunities through creative and efficient use of resources.

Category tactics-

Tactics are methods to attain the best advantage and edge and centre on the areas of assortment pricing , space planning, promotions etc.

Plan implementation-

A specific implementation schedule is developed and responsibilities are assigned

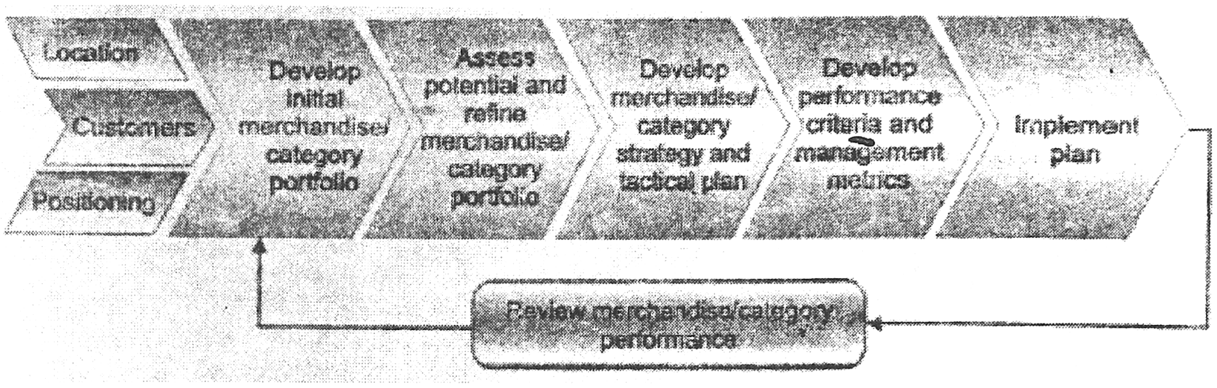
Review-

Reviewing of the progress, and of the actual achievements, as against the targets set for the category. Review aids in the taking of decisions at the right point of time.

Successful category management in retailing is a customer driven process. It enables the retailer to have the right category mix through the preparation and implementation of an efficient category plan.

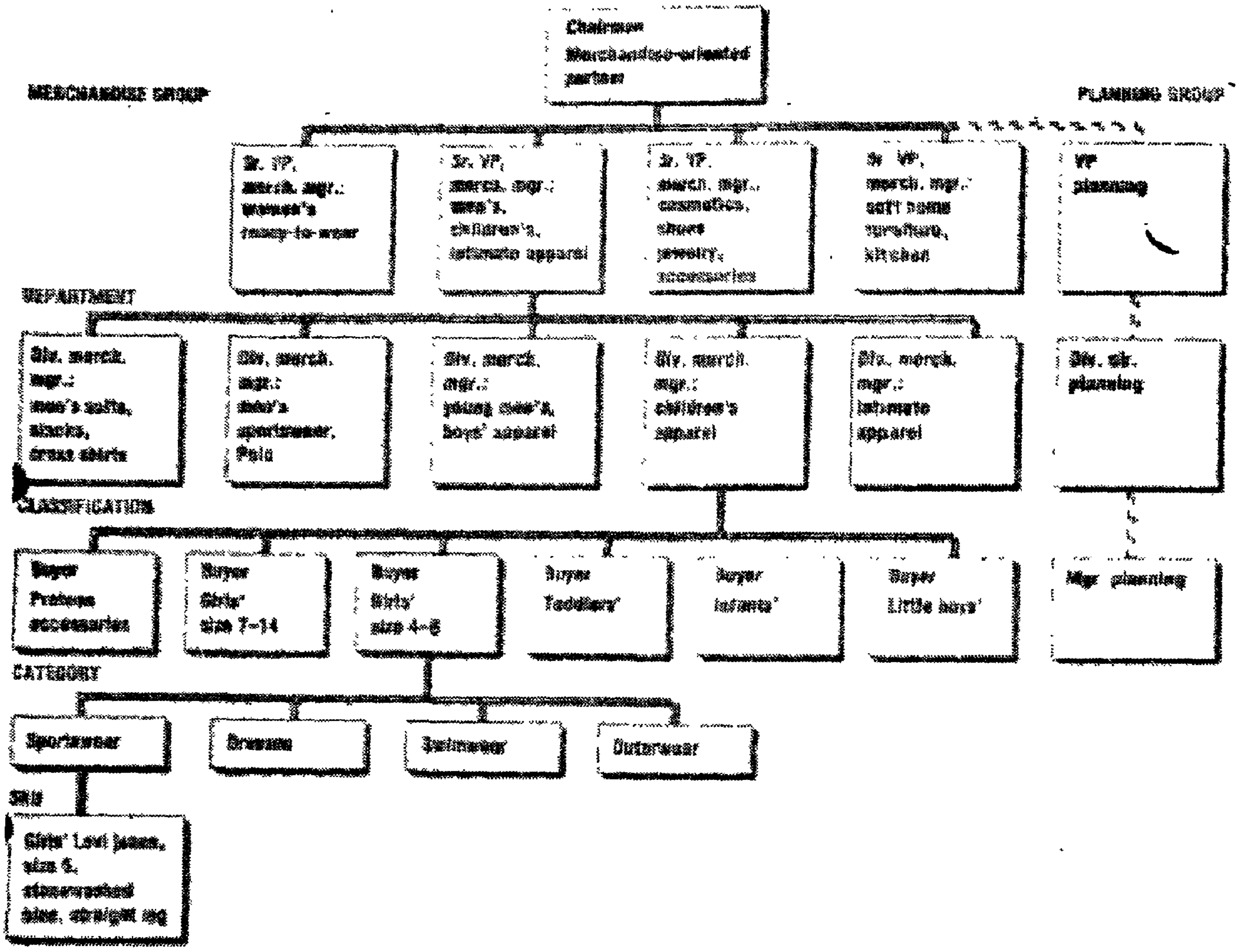
1.13 Category management – the Indian scenario

Indian retail market is at the stage of evolution and not an mature market. Only 1 % of the retail potential is capitalized by 2006 in India. Retailers are still determining the formats that would work in India. Hence in India the category management process would start with identifying the target customers and developing a portfolio for them, refine it, develop strategy and new measurement metrics and then to implement and review. It is clearly defined in the chart below



1.14 The Buyer organization.

It is necessary to understand where in the buying organization the category fits. Here is an exhibit of a simulated merchandise classification scheme of large retail organization



Merchandise group –

The merchandise group is managed by the senior vice president or the General Merchandise Managers (GMM) They are responsible for several departments under their control.

Department –

The departments are managed by Divisional Merchandise Managers who report to the GMM's / Sr Vp. They are responsible for a particular department.

Classification-

Each divisional merchandise manager is responsible for a number of buyers or category managers.

Categories – each buyer purchases a number of categories .

Stock keeping Unit (SKU) It's the smallest unit available for keeping inventory control.

1.15 Summary-

Initial process of merchandise management is that, the retailers and suppliers need to identify consumer needs and to meet those needs effectively. Category management is the result of a set of business conditions that have increasingly challenged many traditional management methods. By focusing on a superior understanding of consumer needs category management provides renewed opportunities for meeting consumer needs and at the same time for achieving competitive advantage as well as lower costs through greater work process efficiencies.

Check Your Progress Questions:

1. Which word provides the origin for the word 'Retail'?
2. What are the 7 R's of Merchandising?
3. What are the several rungs in the Merchandise Hierarchy?
4. What are the factors affecting Merchandise Function?
5. What are the steps involved in Merchandise Planning?
6. Who is a Category Captain?
7. What are the components of Category management?
8. What are the steps in Category Management in Indian Context?
9. What are the echelons in the Buying Organization?

1.16 Answer to 'Check Your Progress' Questions

1.'Retailer' the French word provides the origin for the word 'Retail' which means to break a bulk.

2.Merchandise management is a process by which the retailer accepts to offers the 7^{Rs} of merchandising: the right product, the right place, the right quantity, the right quality, the right price, the right mix or assortment and the right time

3.The several rungs in merchandise hierarchy are Division, Department, Category, Sub Category, Brand , Style and Options.

4.The factors affecting merchandise function are : Size of the organization, Merchandise to be carried, organization structure and the type of the store.

5.Steps in merchandise planning involve Forecasting sales, Defining merchandise requirement, Controlling merchandise and Planning Assortment.

6.Some retailer's turn to one favored vendor to help them manage a particular category is called the Category Captain.

7.Category Management process include Category Definition, Role, assortment, Scorecard, Strategy, Tactics and Plan Implementation.

8.An Indianised process of category management includes Developing initial merchandise, refine them, develop merchandise and performance criteria and implement plan.

9.The rungs in Buying Organization are Merchandise Group, Department, Classification , Categories and Stock Keeping Unit(SKU).

1.17 Exercise and Questions:

1.Briefly explain the concept of Retailing and the functions related to Retail Management.

2.Elaborate on Merchandise Management Process.

3.Describe Category management Process and Organization of Buying by Category.

1.19 Further Readings:

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985

Unit – 2

Structure:

2.0 Introduction
2.1Unit Objectives
2.2 Gross Margin Return On Inventory (GMROI)
2.3 Average Inventory Calculation
2.4 Advantages of High Inventory Turnover
2.5 Disadvantages of High Inventory Turnover
2.6 Category Life Cycle and Sales Forecast
2.7 Developing a Sales Forecast
2.8 Sources of information for Category level forecast
2.9 Stores level forecast
2.10 Planning inventory
2.11Methods of inventory planning
2.12 Summary
2.13Answers to 'Check Your Progress' Questions
2.14Exercises and Questions
2.15Further Readings

2.0 Introduction

Retailers cannot hope to be financially successful unless they preplan the financial plans, start at the top of the retail organization and are broken down into categories, while buyers and merchandise planners develop their own plans and negotiate up the organization.

The resulting merchandise plan is a financial buying blueprint for each category. It considers the firm's financial objectives along with sales projections and merchandise flows. The merchandise plan tells the buyers and planner how much money to spend on a particular category of merchandise in each month so that the sales forecast and other financial objectives are met . Once the merchandise plan is set , the buyers and planners develop the assortment plan. The buyers work with vendors choosing merchandise, negotiating prices, and developing promotions. The merchandise planners break down the over all financial plan into ,how many of each item to purchase and how they should be allocated to stores.

There's a great deal of negotiating at each step. Merchandise managers and buyers compete with each other the size of their merchandise budgets. If they increase their sales forecasts, they will get more money to spend on merchandise. Buyers and merchandise managers have to plan elaborate presentations to convince their superiors to increase their merchandise budgets. Of course, they must be accurate in their projections. If they succeed in having a larger sales forecast approved, and the merchandise doesn't sell, their profitability- and their performance evaluation-will suffer and future forecasts will be questioned.

2.1Unit Objectives

- Understanding GMROI and Average Inventory
- Discussing advantages and disadvantages of Inventory Turnover
- Discussing Category life cycle and Sales forecasting
- Discussing various methods of Inventory planning

2.2 Putting Margin, Sales, and Turnover Together: GMROI

At the corporate level, return on assets is used to plan and evaluate performance of overall retail operations

Return on assets = Net profit margin x Asset turnover

With the strategic profit model, one can use return on assets to plan and compare the performance of executives since they are responsible for managing all of the retailer's assets and realizing a return based on these assets.

But merchandise managers have control over only the merchandise they buy and manage. Buyers generally have control over gross margin but not expenses involved with the operation of the stores and the management of the retailer's human resources, locations, and systems. As a result, the financial ratio that is useful for planning and measuring performance is a return on investment measure called gross margin return on

inventory investment, or GMROI. It measures how many gross margin rupee are earned on every rupee of inventory investment.

GMROI is a similar concept to return on assets, only its components are under the control of the buyer rather than other managers. Instead of combining net profit margins and asset turnover, GMROI uses gross margin percentage and the sales-to- stock ratio, which is similar to inventory turnover.

GMROI= Gross margin percentage x Sales-to-stock ratio

Average inventory in GMROI is measured at cost, because a retailer's investment in inventory is at cost ,not in its retail value.

Like return on assets, GMROI combines the effects of both profits and turnover. It's important to use a measure that considers both of these factors. Departments (such as dairy products)are low margin/high turnover. If the wine department's performance is compared to that of dairy products using inventory turnover alone, the contribution of wine to the supermarket's performance will be undervalued. On the other hand, if only gross margin is used, wine's contribution will be overvalued.

2.3 Calculating Average Inventory

Average inventory is calculated by dividing the sum of the inventory for each of several months by the number of months.

Average inventory= End of the months inventory of the period/Number of months

But how many months should be used? How could we determine the inventory for the month? One approach is to take the end-of – months (EOM) inventories for several months and divide by the number of months available. For example,

Month	Retail Value of Inventory
EDM January	**22,000**
EDM February	**33,000**
EDM March	**38,000**
Total inventory	**93,000**
Average inventory= 93,000/3	**= 31,000**

This approach is adequate only if the end-of –month figure doesn't differ in any appreciable or systematic way from any other day. For instance, January's end-of-month inventory is significantly lower than the other two since it represents the inventory position at the end of the winter clearance sale and before the spring buildup.

Most retailers no longer need to use physical counts to determine average inventory. Point-of- sale terminals capture daily sales and automatically subtract them from on hand inventory. Retailers with POS systems can get accurate average inventory estimates by averaging the inventory on hand for each day in the year. Retailers do typically take occasional physical inventories ,usually twice a year, to determine the amount of inventory shrinkage due to theft or paperwork/ entry mistakes.

2.4 Advantages of High Inventory Turnover

Retailers want rapid inventory turnover but not too rapid , Advantages of rapid inventory include increased sales volume, less risk of obsolescence and markdowns improved salesperson morale, more money for markup opportunities, decreased operating expenses, and increased asset turnover.

- **Increased sales volume**

A rapid inventory turnover increases sales volume since fresh merchandise is available to customers and fresh merchandise sells better and faster than old shopworn merchandise.

Less Risk of obsolescence and Markdowns The value of fashion and other perishable is said to start declining as soon as it's placed on display when inventory is selling quickly merchandise isn't in the store long enough to become obsolete, As a result markdowns are reduced and gross margins increase.

Improved Salesperson Morale With rapid inventory turnover and the fresh merchandise that results, salesperson morale stays high. No one likes to sell yesterday's merchandise. When sales people's morale is high, they try harder so sales increase which increases inventory turnover even further.

More Money for Market opportunities When inventory turnover is high, money previously tied up in inventory is freed to buy more merchandise. Having money available to buy merchandise late in fashion season can open tremendous profit opportunities.

Decreased operating expenses An increase in turnover may mean that a lower level of inventory is supporting the same level of sales. And lower inventory means lower inventory carrying costs, which is an operating expense.

Increased Asset turnover Finally since inventory is current asset and if assets decrease and sales stay the same or increase then asset turnover increases. This directly affects return on assets the key performance measure for top management.

2.5 Disadvantages of Too High inventory Turnover

Retailers should strike a balance in their rate of inventory turnover. An excessively rapid inventory turnover can hurt the firm to a lower sales volume and increase in the cost of good sold and an increase in operating expenses.

Lowered sales volume one way to increase turnover is to limit the number of merchandise categories or the number of SKU s within a category But if customers can't find the size or color they seek or even worse if they can't find the product line at all a

sale is lost. Customers who are disappointed on a regular basis will shop elsewhere and will possibly urge their friends to do the same. In this case not only is a sale lost but so are the customers and their friends.

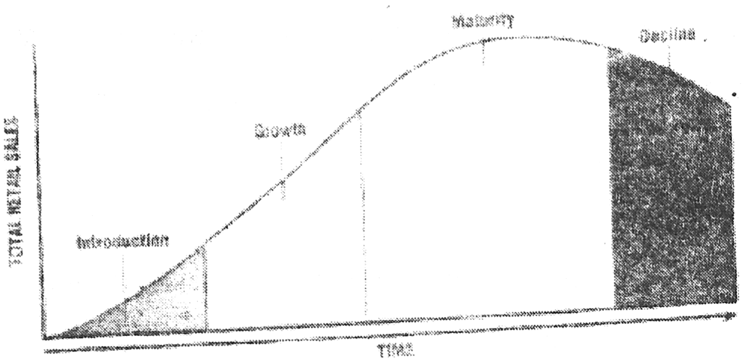
Increased cost of Goods Sold To achieve rapid turnover merchandise must be bought more often and in smaller quantities, which reduces average inventory with out reducing sales. But by buying smaller quantities affects economies of scale, It may be possible for instance, to buy a year's supply of Levi's at a quantity discount that offsets the high costs of carrying a large inventory.

Increased Operating Expenses Economics of scale can also be gained when a retailer purchases large quantities. A buyer spends about the same amount of time meeting with vendors and writing orders whether the order is large or small. It also takes about the same amount of time for both large and small orders to print invoices receive merchandises and pay invoices. All these factors increases merchandise cost.

2.6 Category Life Cycles & Scales forecast

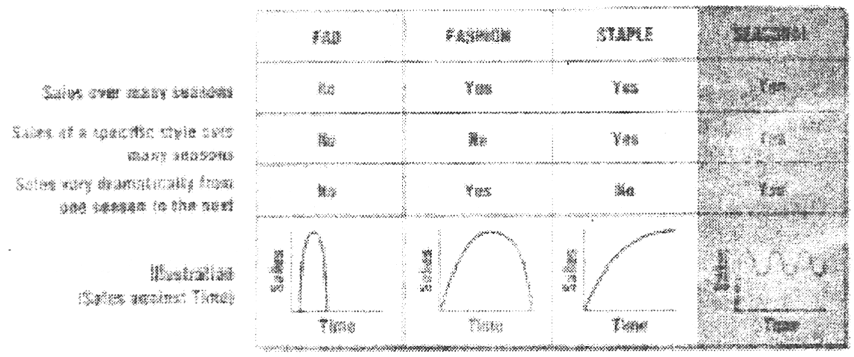
When developing a sales forecast, a retailer must be able to predict how well product categories will sell over time. Product categories typically follow a predictable sales pattern. Sales start off low , increase, plateau and then ultimately decline.

The category life cycle describes a merchandise category's sales pattern over time The category life cycle is divided into four stages. Introduction, growth , maturity and decline. It is important to developing a sales forecast and merchandises based on the lifecycle stage.



Category Life Cycle (CLC)

Variations on the Category Life cycle Most categories follow the basic form of the category life cycle, sales increases to peak and then decline. There are few Variations on the category life cycle –fad, fashion, staple, and season. The distinguishing characteristics between them are whether the category lasts for many seasons, whether a specific style sells for many seasons and whether sales vary dramatically from one to the next.



	FAD	FASHION	STAPLE	SEASONAL
Sales over many seasons	No	Yes	Yes	Yes
Sales of a specific style sells many seasons	No	No	Yes	Yes
Sales vary dramatically from one season to the next	No	Yes	No	Yes
Illustration (Sales against Time)				

A Fad is a merchandise category that generates lot of sales for a relatively short time – often less than a season. Fashion is a category of merchandise that typically lasts several seasons and sales can vary dramatically from one season to the next. The Staple merchandise also called basic merchandise category are in continuous demand over an extended period of time. Even certain brands of basic merchandise however ultimately go into decline. Seasonal merchandise are inventory whose sales vary dramatically according to the time of the year. Both fashion and staple merchandise usually have seasonal influence.

2.7 Developing a Sales Forecast

1. **Reviewing Past Sales** A review of the past sales record is necessary to establish if there is any pattern or trend in the sales figures. A look at the sales figures of the past year for the same period would give an indication of the sales in the current year, given that the conditions are constant.

2. **Analyzing the Changes in the Economics Conditions** It is necessary to take into account the changes happening at the economic front ,as this has a direct link to the consumer spending patterns. Economic slowdowns, increase in unemployment levels etc. all affect business.

3. **Analyzing the Changes in the Sales Potential** It is now necessary to relate the demographic changes in the market to that of the store and the products to be sold.

4. **Analyzing the Changes in the Marketing Strategies of the Retail Organization and the Competition** While creating the sales forecast, it is necessary to take into consideration the marketing strategy to be adopted by the organization and that of the competition. Is there a new line of merchandise to be introduced a new store to be opened or an existing to be remodeled? All these factors need to be taken into consideration.

5. **Creating the sales Forecast** After taking into consideration the above-mentioned points, an estimate of the projected increase in the sales, is arrived at. This is then applied to the various products/ categories, at the projected sales figures.

A sales forecast is thus an outline of what amount of sales need to be achieved, it tells us what amount of sales are targeted and what revenues are expected from those targets. However it does not give the merchandiser any idea of the inventory levels that are required. This brings us to the second stage, which involves the planning of the quantities of merchandise that would be required to achieve the sales forecasted in stages.

A simple way to develop sales forecast for merchandise category is to adjust the past sales to make projections into the future. This type of sales forecasting technique is done at the category level rather than SKU level and is used primarily or fashion merchandise.

2.8 Sources of information for category level forecasts

Buyers utilize a variety of sources in making these decisions.

Previous sales Volume For fashion merchandise where styles changes from year to year. When forecasting sales, retailers must identify real trends (either up or down) and try to isolate a real change in demand from random occurrences . Thus the unusually high and low sales in the prevoius year should be ignored.when trying to forecast sales for the current season.

Published Sources Adjustment to sales trends are based on economic trends in the geograghic area for which the forecast is developed. for example a buyer of a large global store may consider national economic indicators such as the gross national product (GNP) ,interest rates and employment rates where as an independent local clothing store would primarily consider local conditions. Even if national unemployment rates are low they may be significantly higher where a particular retailer has a store if so people may spend less money on fashion in this region than in other areas.

Customer information Customer information can be obtained either by measuring customer reactions to merchandise through sales, by asking customers about customers want today is very helpful in predicting what should be purchased in the future. Obtaining market information about the merchandise directly from the customers is probably the easiest yet most underused method. Some retailers maintain a want book in which salesperson's record out of stock or requested merchandise. Buyers for making purchasing decisions collect this information.

Customer information can be collected through traditional forms of marketing research like depth interviews and focus groups. The depth interview is an unstructured personal interview in which the interviewers use extensive probing to get individual respondents to talk in detail about a subject. For example one grocery store chain goes through the personal checks received each day and selects all customers with large purchase of groceries and several with small purchases. Representatives from the chain call these customers and interview them to find out what they like and don't like about the store.

Another informal method of interviewing customers is to require buyers to spend some time on the selling floor waiting on customers. In most national retail chains buyers are physically isolated from their customers.

A focus group is a small group of respondents interviewed by a moderator using a loosely structured format. Participants are encouraged to express their views and to comment on the views of others in the group. To keep abreast on the teen maker for instance some stores have teen boards comprised of opinion leaders that meet and discusses merchandising and other store related issues.

Vendors and Resident Buying office buyers must seek information from vendors and resident buying officers. Resident buying offices either are independent organizations or are directly associated with particular retailers that office a number of services associated with the procurement of merchandise. Vendors and resident buying officers are excellent sources of market information. They know what's selling in markets around the world.

2.9 Store Level Forecasting

As retailers respond to increased competition oversaturated markets and shoppers who want more of everything for less, it is becoming increasingly important for retailers to become more efficient and quickly tailor merchandise offerings to meet the needs and desires of smaller market segments. To do this requires the merchandise planner to predict sales at the store SKU level. Buyers at more aggregate levels like a region or a distribution center servicing many stores performed the forecasting method described in the previous section and it was done by category not by SKU. The problem with forecasting at more aggregate levels is that store- level variability gets averaged or summed out of the data. This for example happens when one store sells more single serving sized food products and a different store sells family sized products. Combining results from the two stores results in demand data that report evenly distributed sales. Hence SKU level forecasting will be much helpful in deciding appropriate levels of merchandise for respective stores.

2.10 Planning Inventory:

After the sales forecasting exercise has been completed inventory levels needs to be planned. The merchandise budget is the first stage in the planning of merchandise. It is a financial plan which gives an indication of how much to invest in product inventories stated in monetary terms.

The merchandise budget usually comprises five parts.

1. The sales plan i.e. how much of each product needs to be sold, this may be department wise division wise or store wise.
2. The stock support plan, which tells us how much inventory or stock, is needed to achieve those sales.
3. The planned reductions, which may need to be made in case, the product does not sell.
4. The planned purchase levels i. e the quantity of each product that needs to be produced from the market.

5. The Gross Margins The difference between sales and cost of goods sold. That the department division or store contributes to the overall profitability of the company.

2.11 Methods of inventory planning

In order to be able to proceed with merchandise planning needs to be effective. The four methods given below can be best serve the purpose.

1. The basic stock Method.
2. The percentage variation Method.
3. The weeks supply method and
4. The Stocks/ sales Ratio Method.

The Basic Stock method

This method of inventory planning is used when the retailer believes that it is necessary to have a given level of inventory on hand, at all times. Basic stock is the minimum amount of inventory that needs to be maintained for a product, category or store, even during times of low sales.

It is calculated as under:

Basic Stock = Average stock for the season – Average monthly sales for the season, where

Average monthly sales for the season = Total planned sales for the season/ Number of months in the season

Average stock for the season = Total Planned Sales for the season/ Estimated Inventory Turnover Rate for the season

Beginning of Month (BOM) stock = Planned Monthly Sales + Basic Stock

Illustration: Using the basic stock method, calculate BOM inventory for the month of January, given the following information:

Planned sales for the month of January : 30,000

Average monthly sales : 25,000

Average monthly inventory : 40,000

Basic Stock = 40,000 – 25,000 = 15,000

BOM Stock = 30,000+ 15,000 = 45,000

The Percentage variation Method :

This method is normally used when the stock turnover rate is more than six times a year. The basic premise behind this method of inventory planning is that the inventory levels should reflect the actual sales. It is calculated as under:

BOM Stock = Avg Stock for season ½ [1+ (Planned Sales for the month / Average monthly Sales)]

Illustration: Using the Percentage Variation Method, calculate the BOM inventory for the month of January, given the following information:

Planned Sales for the month of January : 30,000

Average monthly Sales : 25,000

Average monthly inventory : 40,000

BOM Stock = Avg Stock for season ½ [1+(Planned sales for the month / Average monthly sales)]

BOM Stock = 40,000 ½ (1+30,000/25,000)

= 40,000 ½ (1+1.2)

= 40,000 *1.1 = 44,000

Week's Supply Method

Retailers such as grocers, who plan inventories on a weekly, and not on a monthly basis, and whose sales do not fluctuate substantially, largely follow the week's supply Method. It is calculated as under:

Number of Weeks to be Stocked = the number of Weeks in the period / Stock turnover rate for the period

Average Weekly Sales = Estimated Total Sales for the period / The Number of Weeks in the period

BOM Stock = Average Weekly Sales /Number of Weeks to be Stocked

Stock to Sales Ratio Method

This method is very easy to use, but it requires the retailer to have a beginning of the month stock, sales ratio. It involves the maintaining of the inventory levels at a specific ratio to the sales. This ratio tells the retailer how much inventory is needed at the beginning of the month, to support the month's estimated sales.

Stock-Sales Ratio = Value of Inventory / Actual Sales

Planned BOM Inventory = Stock- Sales Ratio Planned Sales.

Illustration: Using the Stock to Sales Ratio Method, Calculate the BOM inventory for the month of January, given the following information.

Stock to Sales Ratio = 1.4

Planned Sales for the month of January : 20,000

Planned BOM Inventory = 1.4* 20,000

= 28,000

The Stock Turnover rate

An effective measure of the speed with which products or merchandise moves in and out of a retail store for a given period, is the Stock Turnover rate. It is a measure of efficiency and out of a retail store for a given period, is the Stock Turnover rate. It is a measure of efficiency and is usually calculated for a period, of six months or a year. It is calculated using the following formula:

Planned Sales (for a period)/
Planned Average Inventory (for the period) =Stock Turnover

The stock turnover rate is a measure of efficiency. Every department usually, has its own stock turnover rate, as different merchandise need different speeds of selling. Typically, for grocery products, the stock turnover rates needed would be much higher, as compared to those needed for products like apparel or toys. From the management's perspective, the stock turnover repeating indicates the level of capital usage, i.e., turning money to inventory, inventory to money and then repeating the process again.

2.12 Summary

GMROI project how many gross margin rupee earned on every rupee of inventory expended. It is apparent that there are advantages as well as disadvantages of high inventory turnover. Hence a proper forecast is required at category level as well as stores level for maintaining optimum inventory. And for such an optimum inventory planning various methods of inventory planning is commonly followed such as Basic Stock method, Percentage Variation method, Week Supply Method and Sales Ratio Method.

Check your Progress Questions

1.What are the components of GMROI.

2. How do we calculate Average inventory?

3. What are the variations in Category life Cycle?

4.What are the steps involved in Sales Forecasting?

5.What are the sources of information of Category level forecasting?

6.What are the methods of inventory planning?

2.13 Answer to 'Check Your Progress' Questions.

1.The components of GMROI are Margin , Sales and Turnover.

2. Average inventory can be calculated by Adding End of the month inventory of several months divided by number of months.

3.Few variations in Category Life cycle are Fad, Fashion, Staple and Season.

4.Steps in developing a sales forecast are Reviewing past sales, Analyzing changes in economic condition , sales potential and marketing strategies of the retail organization and competition and creating sales forecast.

5.Various sources of Category level forecast are : Previous sales volume, Published sources, Customer information and vendor buying offices.

6.Commonly used methods of inventory planning are: Basic stock method, Percentage variation method, Weeks supply method, and Stocks/Sales Ratio method.

2.14 Exercises and Questions

1.Illustrate with an example the calculation of GMROI.

2. What are the various methods of inventory planning? Explain with example.

3.Describe Category life cycle and variations to it.

4.Explain the pros and cons of high inventory turnover.

5.Enumerate the steps involved in Sales forecasting.

2.16 Further Readings

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985

UNIT - 3

Structure:

3.0 Introduction
3.1Unit Objectives
3.2 Assortment Plan
3.3 Variety
3.4 Assortment
3.5 Summary
3.6 Answers to 'Check Your Progress' Questions
3.7 Exercise and Questions
3.8 Further Readings

3.0 Introduction

After setting financial goals and determining the relative Importance of variety assortment and product availability the retailer is ready to determine what merchandise to stock using an assortment plan describes in general terms what should be carried in a particular merchandise category. The assortment plan for fashion merchandise doesn't identify specific SKU s since fashions change from year to year , The more fashion – oriented the category ,the less detail will be found in the assortment plan because the merchandise planner requires more flexibility to adjust to fashion changes.

3.1Unit Objectives

- Understanding the Assortment Plan
- Differentiating Variety and Assortment

3.2 Assortment Plan

Historical precedence is the starting point for developing the assortment plan for the current season. The merchandise planner uses the sales, GMROI , and turnover forecast along with the assortment plan from the previous season to develop the plan for the current season. Adjustments are then made based on the merchandise planner's

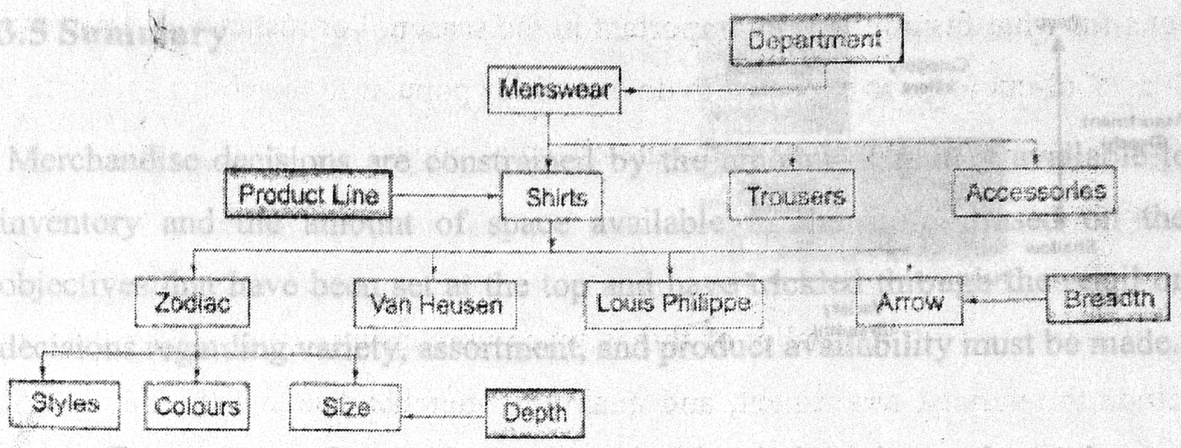
expectations for what fashion will be important in the season. For instance if a particular style such as boot-cut jeans is expected to do especially popular in the coming season, the merchandise planner will give more of the merchandise budget for that style and cut back on traditional jeans.

The retailer looks for a number of things when purchasing inventory for the store. These include the variety, assortment, and quality of merchandise and the merchandise price points, which in combination are referred to as the merchandise mix. The overall key to effective merchandise planning is to ensure that the merchandise mix meets or exceeds the needs and wants of the retailer's market. Once again the retailer should access the situation analysis and target market data to verify that the merchandise is indeed a good fit for the targeted customers.

3.3 VARIETY

The number of product lines (categories) the retailer stocks is referred to as the variety, or breadth. Breadth can also refer to the number of brands carried within a product line. For example, shoe retailers need to decide whether to carry just athletic shoes, work shoes, and boots or to offer a wider variety of products including dress shoes. They also must decide whether to carry a limited assortment of shoe accessories or a full line of shoe accessories.

Breadth is often described along a continum of narrow or broad. A store that offers twenty; lines of shoes may be said to have broad variety; (breadth). In contrast, a store that offers only one line may be said to offer a narrow variety (breadth). The merchandise variety must be consistent with the retailer's mission and vision, and should be developed with he retailer's objectives in mind. The customer will make a number of decisions about the retailer based on the merchandise mix.



3.4 ASSORTMENT

Merchandise assortment, or depth, consists of the stock keeping units (SKUs) within a category (this could include type of brands, colors, and sizes that the retailer stocks within each line it carries). Depth is often described along a continuum of shallow to deep.

Merchandise depth is directly related to quantity, assortment, and variety of merchandise offered. To monitor merchandise depth, retailers use stock-keeping units, or SKUs, to determine the average quantity of merchandise carried for each of the various brands sold in their stores. An SKU is the smallest unit of measure used to inventory products. SKUs are established by the retailer and are typically an alpha-numeric combination. For example, a shirt of a particular style and color could have an SKU of 091766-B, meaning "style number 091766, in blue." An SKU tells the retailer's exactly what product is in inventory. The SKU may or may not be visible to the customer.

The retailer must let the buyer know the assortment policy so that the buyer can develop a merchandise mix that is in line with the retailer's mission, vision, and objectives.

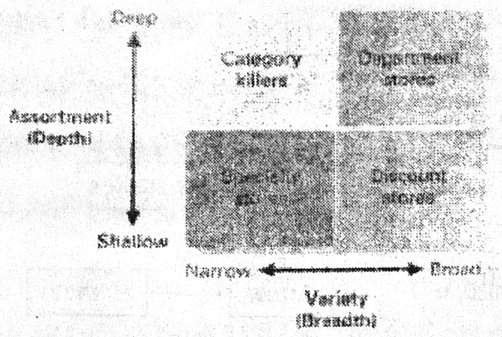


Figure above shows the relationship between variety and assortment. By cross classifying assortment (deep or shallow) by the variety (narrow or broad),a two-by – two dimensional matrix is formed, as depicted in the figure. The four cells in the matrix may; be described as follows:

1. Deep and narrow: many types of goods in one or a few product lines. Examples: category killers (e.g., Toys "R" Us, PETsMart).
2. Shallow and narrow: Few types of goods in one or few product lines. Examples: specialty stores (e.g., Rocky Mountain Chocolate Factory, Kaufman's Tall and Big Men's Shop).
3. Deep and broad: many types of goods in each of many different product lines. Examples: department Stores (e.g., JC Penney, Macy's Sears).
4. Shallow and broad: Few types of goods in each of several different product lines. Example: discount stores (e.g., Wal-Mart, Kmart, Target).

Each individual brand can have its own level of depth. For example consider a shoe retailer that carries the Action shoe. For example brand of Action the retailer must decide which sizes, or depth of offering, to include. Many retailers carry only the most popular sizes and colors of Action so they can have faster inventory turnover (Shallow assortment). Other retailers that focus on customers will be able to find a particular brand of Action shoe in their size and preferred color.

3.5 Summary

Merchandise decisions are constrained by the amount of money available to invest in inventory and the amount of space available in the store. Based on the financial objectives that have been set at the top and have trickled through the retail organization decisions regarding variety, assortment, and product availability must be made.

Variety

Variety is the number of different merchandising categories within a store or department . Stores with a large variety are said to have good breadth – the terms variety and breadth are often used interchangeably.

Assortment

Assortment is the number of SKUs within a category. Stores with large assortments are said to have good depth-the terms assortment and depth are also used interchangeably

Check Your Progress Questions

1.Which provides a base for assortment plan?
2. What are the four type of relationship between Variety and Assortment?

3.6 Answer to 'Check Your Progress' Questions.

1.Sales, GMROI, Historical Precedence and Turnover forecast provides the base for planning assortment for future.
2.The four type of relation ship between Variety and Assortment are: Deep and Narrow, Shallow and Narrow, Deep and Broad, Shallow and Broad.

3.7 Exercise and Questions

1.Describe elaborately the assortment Planning Process and the components to it. Also explain the relationship between those components of a assortment plan.

2.Illustrate the assortment planning process with an example of your choice of an retail organization.

3.8 Further Readings

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985

Unit - 4

Structure:

4.0 Introduction
4.1Unit Objectives
4.2 Dimensions and Constraints of an Optimal Merchandise Mix
4.3 Trade offs between Variety, Assortment and Product Availability.
4.4 Determining Variety and Assortment
4.5 Determining Product availability
4.6 Summary
4.7 Answers to ' Check Your Progress' Questions.
4.8 Exercises and Questions
4.9 Further Readings.

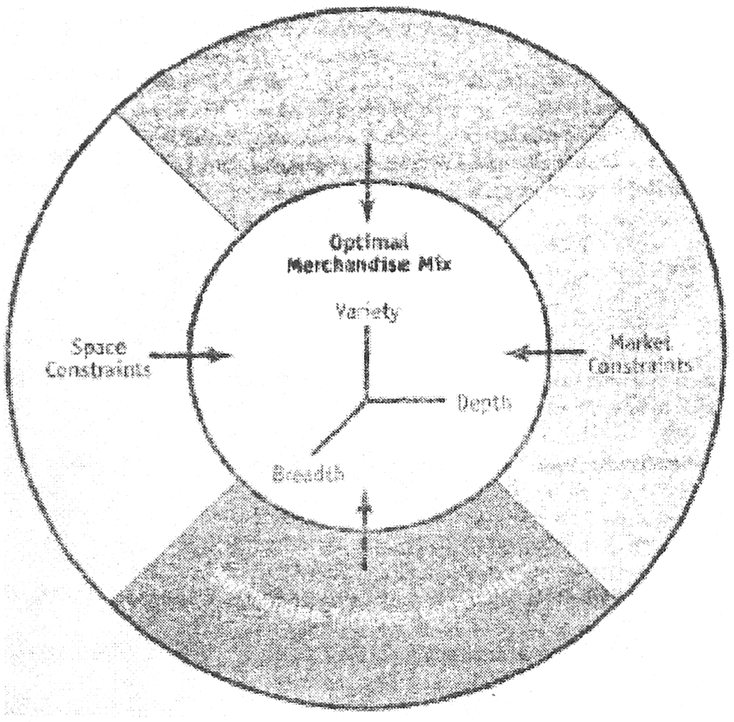
4.0 Introduction

A merchandise line consists of a group of products that are closely related because they are intended for the same end use (all televisions), are sold to the same customer group (junior miss clothing), or fall within a given price range (budge women's wear). Today, for example, over 90 percent of grocery retailers use the term c ıtegory management to refer to their management of categories, or lines, as a strategic business unit. That is, a super market buyer using category management, would no longer be concerned with GMROI for just the Tide or Surf detergent. Today, that buyer would be concerned with the GMROI for the entire detergent line or category. For that buyer, the line or category is his or her strategic business unit. The variety, assortment and product availability trade off is most important to ensure the planned GMROI.

4.1Unit Objectives

- Analyzing the Trade off between Variety , Assortment and Product Availability.
- Understanding factors involved in determining Variety and Assortment.
- Understanding the factors responsible to determine Product availability.

4.2 Dimensions and constraints of an optimal merchandising Mix



The variety of the merchandise mix refers to the number of different lines the retailer stocks in the store. For example department stores have a large variety if merchandise lines. Some have more than 100 departments, carrying such lines as men wear. Women's wear, children's clothing, Infant's wear, toys, Sporting goods, appliances, cosmetics, and household goods. On the other hand, a specialty chain carries only one basic merchandise line office supplies. In the middle of these two would be a retailer sports mart, which sells a complete range of sporting goods.

Breadth also called assortment refers to the number of merchandise brands that are found in the merchandise line. For example a supermarket will have a large amount of breadth, or assortment in the number of different brand of mustard that it carries. Six or seven, national or regional brands and private brand.

Convenience store, however will offer very little breadth in that it will generally carry only one or two brands in any merchandise line.

Breadth is especially a problem for retailers selling private. Label brands. Retailers need to achieve a proper balance between their own private label and the national brands. However, sometimes-powerful manufacturer may try to tie some of its merchandise lines together. That is if the retailer must carry the manufacturer's entire product line. But because private label brands offer retailers a lower cost and a higher gross margin, retailers generally do not want to carry the manufacturer's entails a lower cost and a higher gross margin, retailers generally do not want to carry the manufacturer's complete line. A battle of the brands occurs when retailers in determining the breath of the product assortment. Have their own products competing with manufacturer's products for shelf space and control over display location. One of the consequences of the battle of the brands is that many retailers are now stocking either one or both of the top brands in a product line or category and their own private brand. As a result many " third tier" brands have been left off the store's shelves.

4.3 Traded – offs between variety, Assortment, and product Availability

How do retailers make the trade –off between varieties, assortment and product availability it depends on their particular marketing strategy. A retail strategy identifies (1) the target market toward which a retailer plans to commit its resources. (2) the nature of the retail offering that the retailer plans to use to satisfy the target market's needs. And (3) the bases upon which the retailer will attempt to build a sustainable competitive advantage.

If any of these three elements – variety, assortment, or product availability – aren't what the customer expects or needs, a retailer will likely lose the sale and possibly the customer.

The trade – offs between variety assortment and product availability are strategic issues, of the three issues, variety is the most strategic. Variety is most important in defining the retailer in the customer's eyes.

Variety also defines the retailer's vendor structure. Does it purchase form many different types of manufacturers or just a few? Finally, decisions regarding variety are typically made assortment or product availability. Top managers, for instance, make decision about whether to delete categories or even departments from the sore. Since these decisions have important ramifications, they're made only after serious consideration.

4.4 Determining variety and Assortment

In attempting to determine the variety and assortment for a category like jeans the buyer would consider the following factor profitability of the merchandise mix , the corporate philosophy towards the assortment, physical characteristics of the store, layout of the internet site, balance between too much versus too little assortment, and the degree to which categories of merchandise complement each other.

Profitability of Merchandise Mix

Since retailers are constrained by the amount of money, they have to invest in merchandise and space to put the merchandise in, they're always trying to find the most profitable mix of products.

Corporate strategy and positioning toward the Assortment

The corporate strategy toward the assortment ,the buyer determine the number of style and colors to purchase. Another issue is whether top management wants to grow or shrink a particular merchandise category. Some department stores, for instance, have dropped furniture and major appliance altogether because of low turnover, low profit margins, or lack of space. Many stores however have taken a fairly aggressive stance on men's sportswear in recent years. So even if a category is shrinking if the retailer's overall strategy is to enlarge the department the category could be expanded.

By the same token websites must be designed so that the customer can easily navigate through them. If there are too many choices. If the merchandise is organized in a

a less than obvious fashion if the customer perceives the site to be cluttered or if the checkout process is difficult. Customers click and are off to an other site.

Balance between Too Much versus Too Little Assortment

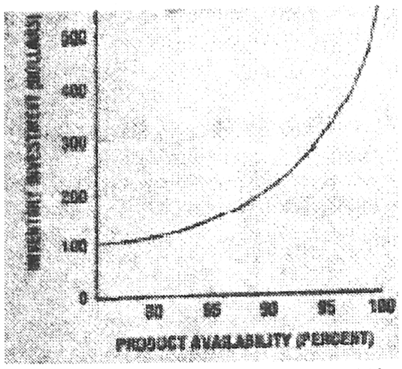
Both traditional retailers and multi channel retailers must contend with the balance between having too much versus too little assortment . In general , retailers must offer enough assortment to satisfy the customer's needs and expectations but not too much so as to confuse them and turn off. An important function of retailers has been to provide a carefully edited selection of merchandise that meets the needs of their target customers.

Recent research has shown that customers actually buy more if there are modest reductions of redundant items made to assortments. Such as different sizes of ketchup in a supermarket, deep cuts in the assortment size. However lead to sales declines, in the end size of the assortment depends on the target markets expectations, Is to provide customers with a carefully edited assortment or one stop shopping. Second, how effective is the multi channel retailer in guiding customers through its website with tailored and adaptive search and develop a search engine that is good at suggesting additional purchases given past purchase behavior then expanded assortments should have a positive benefit.

Complementary merchandise

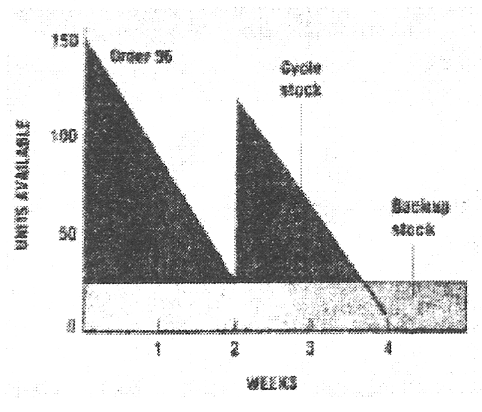
When retailers plan to add to their assortment they must consider whether the merchandise under consideration complements other merchandise in the department. Internet retailers have the advantage of being able to easily suggest complementary products.

4.5 Determining product Availability



Investment – Product availability Tradeoff

Another important dimension of the assortment planning process is product availability. Recall that product availability defines the percentage of demand for a particular SKU that is satisfied. The higher the product availability, the higher the amount of backup stock necessary to ensure, that the retailer won't be out of stock on a particular SKU when the customer demands. Choosing an appropriate amount of backup stock is critical to successful assortment planning because if the backup stock is too low, the retailer will lose sales, and possibly customers too, scarce financial resources will be wasted in needless inventory that could be more profitably invested in more variety or assortment.



Order level, cycle stock, backup stock requirements

Fluctuations in lead-time also affect the amount of backup stock. But if lead-time is plus or minus one day on one shipment and then plus or minus five days on the next shipment the stores must carry additional backup stock to cover the uncertainty in lead-time. Many retailers using quick response inventory systems are forcing their vendors to

deliver merchandise within a very narrow window something two or three hours to reduce the fluctuations in lead-time and thus the amount of required backup stock. The vendor's product availability also affects the retailer's backup stock requirements.

4.6 Summary

Striking a balance between Variety, Assortment and Product availability is of prime importance in any retail organization. Of the three, variety is deemed to be very important as it defines the retailer in the customer's eye. Various factors affect the designing and optimization of the mix such as Profitability, Corporate strategy etc., If any of the three element variety, assortment and product availability are not what the customer expects or needs, a retailer will likely to lose the sales and possibly the customers.

Check Your Progress Questions

1.What are the three dimensions of an Optimal merchandise mix?
2.What are the components of the retail strategy ?
3. What are the factors involved in determining Variety and Assortment?

4.7 Answers to 'Check Your Progress' Questions

1.The three dimensions of Optimal Merchandise Mix are: Variety, Breadth and Depth.
2. A retail strategy identifies (1) the target market toward which a retailer plans to commit its resources. (2) the nature of the retail offering that the retailer plans to use to satisfy the target market's needs. And (3) the bases upon which the retailer will attempt to build a sustainable competitive advantage.
3.Factors involved in determining Variety and Assortment are: Profitability of merchandise mix, corporate strategy and positioning towards assortment, balance between too much versus too little assortment and Complementary merchandise.

4.8 Exercise and Questions

1.What are the considerations for designing an optimal merchandise mix?

2.Illustrate with practical example the Trade offs between Variety, Assortment and Product availability.

3.Narrate the process of determining Variety , Assortment and Product availability.

4.9 Further Readings

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985

Unit – 5

Structure:

5.0 Introduction
5.1Unit Objectives
5.2 Fashion Merchandise
5.3 Staple Merchandise
5.4 Staple merchandise buying system
5.5 Fashion merchandise buying system
5.6 Summary
5.7 Answers to 'Check Your Progress' Questions
5.8 Exercise and Questions
5.9 Further readings

5.0 Introduction

The type of merchandise that an organization carries also affects the assortment plan of the respective organization. Merchandise may be classified into Basic or Staple Merchandise, Fashion, Convenience or specialty goods. Fashion goods have high demand over short period of time where as staples are basic products with consistent demand. As the demand pattern differs buying system for those products also vary accordingly which is discussed in this chapter.

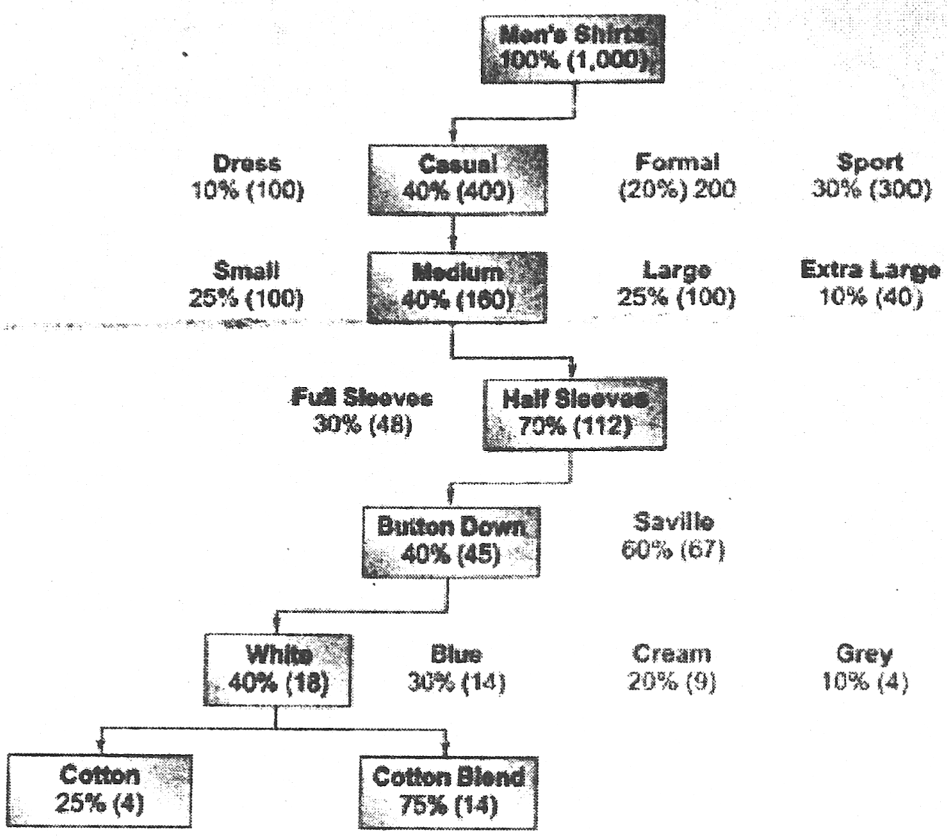
5.1 Unit Objectives

- Understanding Staple and Fashion merchandise
- Discussing staple and fashion merchandise buying systems

5.2 Fashion merchandise

Fashion merchandise have high demand for a relatively short period of time Buying the right quantities at the right time is of great importance for this category of products, as the demand for the product exists for a limited time . Excess buying may result in heavy markdowns at the end of the season or when the product goes out of

style. Examples of such products include various cuts in jeans which may be in style for a season, short lengths in kurtas etc.



5.3 Staple/Basic merchandise

These are products which consumers buy year in and year out. The store would usually require these products, to be in stock at all times. The retailers policies with respect to the type of brands stocked and the level of exclusivity to be maintained in the store, also affect the merchandise buying decisions. Thus after arriving at the amount of money available for investing in the inventory, a merchandiser would have to determine the variety of the merchandise.

Let us take the example of a merchandiser who is working towards the assortment plan for the menswear department for a large retail store. He would start by determining the product line, which is under consideration. A product line is a broad category of product having similar characteristics and uses. Thus in menswear product lines could be

shirts, trousers, accessories, shoes, etc. He would then have to determine the breadth and depth to be offered under the said product line. The breadth refers to the number of brands carried within each product classification. The depth on the other hand refers to the number of choices offered to the customers within each brand or product classification. The same is illustrated on fig .

While a merchandise always works towards creating an optimal merchandise mix, various factors would affect his / her decision. These would be the amount of money actually available for buying the targets set by the merchandise turnover, the space actually available within the stores for stocking the merchandise and the market constraints. Working under these constraints, a buyer works towards creating an optimal merchandise plan.

5.4 STAPLE MERCHANDIES BUYING SYSTEMS

Staple merchandise buying systems are used for merchandise that follows a predictable order-receipt order cycle. These systems are used for buying most of the merchandise found in food and discount stores in addition to some categories in specialty and department stores like underwear, socks and house wears.

The Inventory Management Report

The inventory management report information on sales velocity, inventory available, the amount on order, inventory sales forecast and most important, the quantity to order for each SKU.

The retailer will have a prespecified schedule to each vendor. The schedule is determined by weighting the cost of carrying inventory versus the cost of buying and handling the inventory. The more the retailer purchase at one time the higher the carrying costs but the lower the buying and handling costs.

Although each line has a prespecified schedule for ordering each vendor's inventory status is checked daily. For instance even through Tuperware items may be scheduled to be purchased every five days; occasionally increased demand may dictate that several items need replenishment sooner. The combination of having a prespecifed schedule based on the trade off between inventory carrying and ordering costs and the flexibility to react to demand fluctuations helps to ensure a profitable ordering strategy.

Basic Stock List

The basic stock list describes each SKU and summarizes the inventory position. Specifically it contains the stock number and description of the item. How many items are on hand , and on order , and sales for the past 12 and 4 weeks. The basic stock list defines each SKU in precise rather than general terms. The basic stock list is a necessary component of any management systems.

Inventory Turnover

The planned inventory turnover is based on overall financial goals and drives the inventory management system.

Product Availability

Determining the appropriate planned level of product availability for staple merchandise can be difficult and requires considerable managerial judgment.

Backup stock

Backup stock also known as safety stock or buffer stock is inventory used for guard against going out of stock when demand exceeds forecasts or when merchandise is delayed.

Forecast sales forecasts for staple items is fairly straightforward and mechanical compared to those for fashion merchandise. With fashion merchandise past trends and other issues that help determine the future are examined. Forecasting sales of staple items entails extending sales trends from the past into the future.

Order point the order point is the amount of inventory below, which the quantity available shouldn't go or the item will be out of stock before the next order arrives. The order point in the periodic system is defined as

Order point = [(Demand / Day) (Lead time+ Review time)] + (Backup stock)

The lead-time is the amount of time between recognition that an order needs to be placed and when it arrives in the store and is ready for sale. Assume demand per day is 1 day and lead-time is zero days. (This may be the case in a pharmacy receiving, shipments from its wholesaler more than once a day). Here the order point would be zero. The buyer would wait until stock ran out and then order and replenish the merchandise almost instantaneously.

With lead time of two weeks, there's Some point below which the buyer shouldn't deplete the inventory with out ordering or the retailer would start selling backup stock before the next order arrived. Further the buyer only reviews the line once a week, and 20 units of backup stock are necessary to maintain a high service level, in this case, of demand is 7 units per day then,

Order point = [(7 units) x (20 units) = 167 unites

Here the buyer orders if quantity available falls to 167 units of fewer.

Order Quantity

The question remains How much should the buyer order when the quantity available is less than the order point? He or she should order enough so the cycle stock isn't depleted and sales dip into backup stock before the next order arrives- this is the difference between the quantity available and the order point .

5.5 FASHION MERCHANDISE BUYING SYSTEM

The merchandise budget plan specifies the inventory investment in a category over time. It isn't a complete buying plan since it doesn't indicate the specific assortment to buy or the quantities. The plan just specifies how much money should be spent to support sales and achieve turnover and GMROI objectives.

Actual sales might differ form the sales forecasted in the merchandise budget plan. Even with this uncertainty the plan is used to coordinate the supply and demand for merchandise and to ensure that the financial goals are realized. In addition the plan coordinates the activities of buyer for different merchandise categories, so that there is not too much merchandise in some categories and not enough in others.

Monthly sales Percent Distribution to season

The starting point for determining the percent distribution of sales by month is historical records. The percentage of total sales, that occurs in a particular month's percentage over a few years to check for any significant changes. For instance, the buyer realizes that the autumn selling season for men's tailored shift toward earlier purchasing will affect the percent distribution of sales by month .The distribution may also vary due to changes made by the buyer or the competitor's marketing strategies. The buyer must include special sales that did not occur in the way that they're built into overall sales forecast.

Monthly sales

Monthly sales equal the forecast of total sales for the six-month period multiplied by each sales percentage by month.

Monthly Reductions percent Distribution to season

To have enough merchandise every month to support the monthly sales forecast the buyer must consider factors that reduce the inventory level, although sales are the primary reduction. The value of the inventory is also reduced by markdowns, shrinkage, and discounts to employees. The merchandise budget planning process builds in these additional reductions into planned purchases, otherwise, the retailer would always be under stocked.

Monthly Reductions

The buyer calculates the monthly reductions in the same way as the monthly sales. The total reductions are multiplied by each percentage.

BOM (Beginning of Month) Stock to sales Radio

The stock to sales ratio specifies the amount of inventory that should be on hand at the beginning of the month to support the sales forecast and maintain the inventory turnover objective. The numerator is BOM inventory. Thus a stock to sales radio of 2 means that we plan to have twice as much inventory on hand at the beginning of the month as we plan to sell for that month.

The stock to sales ratios are calculated in four steps

Step 1:

Calculate Sales to stock Ratio that GMROI is equal to the gross percentage times the sales to stock ratio. Where the sales to stock ratio are conceptually of at retail, The GMROI is based on overall corporate financial objectives, and broken down into the gross margin and sales to stock ratio.

GMROI = Gross margin % x Sales –to-stock ratio

122.72%= 45% x 2.727

Note that since we are doing six month rather than an annual plan, the sales to stock ratio is based in six month, rather than annual sales. So for this six-month period, we forecast 2.727 times as much sale as we have invested in cost inventory.

Step 2:

Covert the sales to stock Ratio to Inventory Turnover

Inventory turnover = Sales to stock ratio x (100%-Gross margin %, expressed as decimal)

1.5 = 2.727 x .55

This adjustment is necessary since the sales to stock ratio defines sales at retail and inventory at cost, whereas inventory turnover defines both sales and inventory either at retail or at cost. Like the sales to stock ratio, the inventory turnover is based on a six-month period.

Step 3:

Calculate Average Stock-to- Sales Ratio

Average stock-to-sales ratio = 6 months /Inventory turnover

4 =6 / 1.5

(If preparing a 12month plan, the buyer must divide 12into the annual inventory turnover.) As with inventory turnover, both the numerator and denominator can be either at cost or at retail. Since the merchandise budget plan is based on retail, it's easiest to think of the numerator as BOM retail inventory and the denominator as sales for that month. This to achieve a six-month inventory that's four months of supply or 16 weeks of supply.

Even a buyer must be careful when thinking about the average stock-to –sales ratio. It can be easily confused with the sales –to –stock ratio. One isn't the inverse of the other, however, Sales are the same in both ratios. But stock in the sales-to –stock ratio is the average inventory at cost over all days in the period, whereas stock in the average stock-to- sales ratio is the average BOM inventory at retail. Also, the BOM stock-to-sales ratio is an average for all months. Adjustments are made to this average to account for seasonal variation in sales.

Step 4:

Calculate Monthly Stock-to-Sales Ratios. The monthly stock-to-sales ratio calculated above to achieve the planned inventory turnover, Generally, monthly stock-to –sales ratios vary in the opposite direction of sales. That is, in months when sales are larger, stock-to sales ratios are smaller, and vice versa.

BOM STOCK

The amount of inventory planed for the beginning of the month (BOM) equals

Monthly sales x BOM stock-to –sales ratioWhen doing this multiplication, sales drops out of the equation , leaving BOM stock.

EOM (End-of-Month) Stock

The BOM stock from the current month is the same as the EOM (end-of –month) stock in the previous month.

This formula isn't particularly enlightening, so consider the following explanation. At the beginning of the month, the inventory level equals BOM stock.. During the month, merchandise is sold and various reductions, such as markdowns occur. So BOM stock minus monthly sales minus reductions equals EOM stock if nothing is purchased. But something must be purchased to get back up to the forecast EOM STOCK. The difference between EOM stock if nothing is purchased (BOM stock- sales- reductions) and the forecast EOM stock is the additions to stock.

5.6 Summary

Assortment plan provides a general outline of what type of merchandise should be carried, it doesn't tell you how much to buy. Specifically the above mentioned systems of buying and tools help buyers and merchandise planners determine how much to buy in fashion as well as staple products. This system helps to monitor and measure average current demand, forecast future SKU demand with allowances made for seasonal variations and developing ordering decision rules for optimum restocking.

Check Your Progress Questions

1.Whats the nature of Fashion goods?

2.Whats the nature of Staple goods?

5.7 Answers to 'Check Your Progress' Questions

1.Fashion goods are those, which have high demand for relatively short period of time.

2. Staple goods are those basic products that an organization should carry and they follow consistent demand.

5.8 Exercise and Questions

1.Elaborate the various steps involved in staple merchandise buying system?

2. Describe fashion goods? Illustrate with examples the steps and decisions involved in fashion merchandise buying.

5.9 Further Readings

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985

Unit – 6

Structure:

6.0 Introduction
6.1Unit Objectives
6.2 Budgeting Merchandise
6.3 Approaches to Budgeting
6.4 Elements in Merchandise budgeting process
6.5 Formulas for Budgeting merchandise
6.6 Open to Buy System
6.7 Calculating Open to Buy for past period
6.8 Calculating Open to buy for current period
6.9 Allocating merchandise to stores
6.10 Analysing merchandise performance
6.11 Summary
6.12 Answers to 'Check your Progress' Questions
6.13 Exercise and Questions
6.14 Further Readings

6.0 Introduction

Merchandise consists of the products or services the retailer currently offers, or plans to offer, for sale to customers. Merchandising refers to activities involved in organizing the display of products or services. In a buying sense, *merchandising* refers to the process of buying and selling goods and services to generate profits from the consumer and business markets .To plan for current and future products and services, the retailer needs a good understanding of the costs involved in merchandising and an idea of what consumers will want in the future. These requirements are key to establishing effective merchandise budgets.

6.1Unit Objectives

- Discussing merchandise budgeting process
- Understanding Calculation of open to buy systems
- Learning tools to analyze merchandise performance

6.2 BUDGETING FOR MERCHANDISE AND FORECASTING

To effectively utilize the budgeting process, the retailer needs a fairly comprehensive financial merchandise plan that includes a section *on* performance objectives for finance personnel. In addition, the retailer needs to know which products are to be purchased and in what quantities (forecasting). Many retailers establish plans that allow them to see both the physical product purchases and the rupee spent on those purchases.

Budgets can be prepared for any length of time; the standard is yearly. Many retailers, however, generate budgets on a monthly, quarterly, seasonal, or every-four-week basis. Some retailers prepare budgets on a rolling basis, meaning that if a retailer is budgeting on a four-week basis, another week is added to the budget as one week of the budget period expires. In this way, the budget always includes four weeks.

Although not common, budgets can be prepared for four-month and six month periods. The time period is left to the discretion of the retailer and the company's financial analysts. Retailers often have to purchase inventory six to twelve months in advance, so an inventory plan may be completed well in advance of receipt and stocking of the inventory merchandise. The beginning point for establishing a budget is to set responsibility: Who, specifically, will be responsible for the process?

6.3 Approaches to Budgeting:

Many retailers use budgeting committees or ask for input *from* several departments. Some retailers use a **Bottom-up approach** to budgeting. In this method, each retail department supplies data for the budget; these budgets are then scrutinized and passed *on* to the next level, until the budget finally goes to the individual who is primarily responsible for the budgeting process. Other firms select a more **Top-down approach,** wherein upper management personnel prepare a budget and pass it down to their various departments. The departments are then instructed to try to "stay within budget" when

making merchandise-buying decisions. It is possible to combine the bottom-up and top-down approaches to ensure adequate input from the retailer's employees, yet leaving the final decision making to the financial merchandise expert.

The retailer needs to determine a timeline for putting the budget into effect. Unfortunately, many retailers must order merchandise three to six months, or even a year, before the goods are received and ready for sale. Therefore, a six-month or one-year budget may be necessary. Even if the budget is for six months Or a year, the retailer may want to break it into monthly or even weekly components due to the constantly changing retail environment.

In this way, the accuracy *of* the budget can be determined by comparing the weekly or monthly budgeted amounts to the actual amounts. This approach allows the retailer to either change the product mix, purchase more products that are moving quickly, drop products that are not moving, reduce the price of slow-moving merchandise, or increase the price *of* fast-selling merchandise, to name but a *few* strategies. Whatever the reaction to the budget, developing a budget gives the retailer a method of control and evaluation on an ongoing basis. Therefore, a key to effective budgeting is flexibility.

6.4 Elements in Merchandise Budgeting Process:

Numerous methods have been developed for merchandise budgeting. Most of the methods have common inputs, or variables, that are essential to the retailer and financial planner. The following elements are generally included in the budgeting process:

Planned monthly sales
Planned beginning-of-month (BOM) stock .
Monthly retail reductions .
Planned end-of-month (EOM) stock .
Planned purchases for the month at retail price .

Planned purchases for the month at cost .
Initial markup for the month .
Planned gross margin for the month

To develop a budget, the retailer must forecast planned sales. Sales should be estimated for the entire budget period, but also on a weekly or monthly basis. There are numerous methods for inventory forecasting. The easiest is to look at the past year's performance. Another method is to examine the average of the last two years, the last *five* years, and so *on*. This is a good method as long as adjustments are made *for* changes in the environment that may affect the purchases and forecasts, such as inflation, marketing changes, and the economy.

A forecast should include as many external variables as possible. These variables may include changes in the population mix for a particular retail market, changes in the economy of that market, and changes in any of the environments identified in the situational analysis. Larger firms use computer models (programs) that combine environmental inputs with past sales data. Small firms use a more informal approach, but still take new industries, population changes, and similar factors into account when deciding how much to purchase.

The next step is to assess planned beginning- and end-of-month stock. Because of changes in demand *for* products, retailers generally carry additional supplies of products called safety stock. In retailing it is generally better to carry an additional, "small" amount *of* merchandise to keep from experiencing a stock out situation, in which the retailer runs out of products for which demand still exists.

It is important to reassess optimal stock levels on a frequent basis. Calculating safety stock once a year, instead of several times a year is a common mistake. More frequent calculations help maintain more efficient stock levels. An excellent method *of* determining beginning-of-month (BOM) and end of- month (EOM) stock balances is to calculate a stock-to-sales ratio. A stock to- sales ratio allows a comparison of stock levels

to levels of sales. In other words, the ratio indicates how much stock is needed during a given sales period-say, one month-to prevent a stock shortage. This ratio supports the retailer's forecast. A good way to assess BOM and EOM inventory levels is as follows.

6.5 FORMULAS ON A MONTHLY BUDGETING BASIS:

Planned monthly sales= Planned sales percentage for the month x Planned sales for the month

B0M stock= Planned monthly sales x Planned B0M stock-to-sales ratio

Planned retail reductions= Planned monthly sales x Planned retail reductions in percentages

EOM stock= B0M stock(for the upcoming month)

Planned purchases(at retail = Planned monthly sales+ Planned reductions+ Planned EOM stock- PlannedB0M stock

Planned purchases (at cost= Planned purchases at retail x (100%- Initial markup percentage estimates

Planned initial markup= Planned monthly purchases x Planned markup percentage

Gross margin= Initial markup- Planned reductions

Walgreens Budgeting in a Glance:

Through the use of , point-of-sale (POS) databases. In addition, training and practice helps in the execution of this task. Recall that carrying inventory costs the retailer in two ways. First, the inventory takes up valuable selling space and capital (carrying cost of inventory).

Second, slow-moving or non selling merchandise occupies space that could be given to more current or faster-moving products.

Walgreens is an example of a company that used technology to decrease inventory costs. The drugstore chain improved its strategic inventory management system and thereby cut safety stock and cycle times in its warehouses and stores from 53 days in 2002 to 44 days in 2003. As a result, inventory-carrying costs were reduced by 1.5 billion over three years (2003-2006).

The retailer needs to plan for any retail reductions that may occur during the budget period. As stated earlier, retail reductions are any stock shortages, markdowns, or employee discounts that accrued during the budget forecast period.

Next, purchases must be planned at the selling price and at cost amounts. Finally, the gross margin needs to be added, allowing the retailer to generate profits.As shown in the formulas the retailer can determining the merchandise budget.

To acquire the data necessary to create a budget, the retailer needs to understand the system of inventory valuation used by the company's accountants.

6.6 OPEN-TO-BUY

Open-to-buy is the amount the buyer has left to spend for a given time period, typically a month. Open-to-buy planning helps the retailer keep track of how much money has been expended on inventory for any given period, plus the amount of inventory on hand. In some instances unplanned purchases may come up and the buyer must check open-to-buy records to make sure there is money left in the budget for those purchases.

Reasons for unplanned purchases include the introduction of new products into the market and opportunities to buy at substantial discounts, such as when a supplier is trying to move merchandise to clear its warehouses for new shipments. The retailer must have resources left in the budget to take advantage of sales and markdowns by suppliers.

To calculate open-to-buy, the retailer simply takes the planned purchases and subtracts out any commitments to purchase products (already committed orders):

Open-to-buy (at retail) = Planned purchases - Purchase commitments

6.7 Calculating Open-to-Buy for Past Periods

XYZ co., has the following situation:

The way we view open-to-buy and how It Is calculated vary depending on whether we're looking at a past period or at the current period. Let's start with a past period. We are now in the middle of May-April is over. Notice that there's an entry for actual April EOM stock (Rs59,500), but not one for February. The calculation of open-to-buy at the end of a period is easy. Since the month is over, we know that the actual EOM stock is equal to the projected EOM stock. Open to- buy is zeroed out because there's no point in buying merchandise for a month I that's already over.

Thus, , Projected EOM stock plan =EOM actuals Rs59,500 - Rs59,500

Open-to-buy = 0

6.8 Calculating Open-to-Buy for the Current Period

Now let's look at May, the current month. Notice that there is a BOM stock actual of Rs59,500, but there is no EOM stock actual because the month has started but it hasn't finished. When calculating the open-to-buy for the current month, the projected EOM stock plan comes into play. Think of the projected EOM stock plan as a new and improved estimate of the planned EOM stock from the merchandise budget plan. This new and improved version takes information into I account that wasn't available when the merchandise budget plan was made. The formula for projected EOM stock plan is

Actual BOM stock	59,500
+ Monthly additions actual (what merchandise was actually received)	+ 7,000
+ On order (what is on order for the month)	+ 18,000
- Sales plan	- 15,600
- Monthly reductions plan	- 2,310
Projected EOM stock plan =	Rs66,590

Although this formula may seem complicated, think of it this way: The projected EOM stock is equal to the inventory we have at the beginning of the month plus what we buy minus what we get rid of through sales or other inventory reductions.

The open-to-buy formula used during the current month is simply the difference between what you originally planned to end with from the merchandise budget plan (EOM stock plan) and what you think you will end with based on information collected during the month (projected EOM stock plan): Open-to-buy plan =EOM stock planned - Projected EOM stock Rs2,050 = Rs68,640 - Rs66,590

This means that we have Rs. 2,050 left to spend in February if we want to reach our planned EOM stock of Rs68,640. If the open-to-buy was negative, we would have overspent our budget. As this section's example shows, the assortment planning process can be complicated. In an actual multistore chain, the process is even more complex than in our example. A good assortment plan requires a fine mix of subjective and experienced judgments, a good information system, and a systematic method of keeping historical records. Now lets look at a multi store retailer allocating merchandise to store.

6.9 ALLOCATING MERCHANDISE TO STORES

Once the buyer has purchased either fashion or staple merchandise, the merchandise planner typically allocates it to stores. Retailers utilize historical sales information, but they pay close attention to current supply and demand situations to determine the proper inventory allocation. For instance, if a retailer is having difficulty meeting demand because a vendor is unable to deliver, or if actual sales are lagging behind the forecast, the retailer will have to adjust the historically derived allocation downward.

Every chain's allocation of merchandise to stores is different. A core assortment is a relatively large proportion of the total assortment that is carried by each store in the chain, regardless of size. The core assortment is necessary to maintain 'the image of the chain. If the chain were to cut back the assortment too far in smaller stores, customers would perceive the smaller stores as having an inferior assortment. Hence, smaller stores require a higher-than-average-stock-to-sales ratio. The opposite is true for stores with larger-than-average.

The process of allocating merchandise to stores that we just described is useful for fashion merchandise and new staple items. As merchandise sells, it must be replenished, either by the vendor or through distribution centers. Retailers use either a pull or a push distribution strategy to replenish merchandise. With a pull distribution strategy, orders for merchandise are generated at the store level on the basis of demand data captured by point-of-sale terminals. With a push distribution strategy, merchandise is allocated to the stores on the basis of historical demand, the inventory position at the distribution center, and the needs of the stores. A pull strategy is used by more sophisticated retailers because it's more responsive to customer demand.

6.10 ANALYSING MERCHANDISE PERFORMANCE

ABC Analysis/Pareto rule: ABC analysis ranks merchandise by a predetermined performance measure. This helps determine which items should never be out of stock, which items should occasionally be allowed to be out of stock and which items should be deleted from the stock selection. An ABC analysis can he done at any level, for merchandise classification from Stock Keeping Unit (SKU) to department.

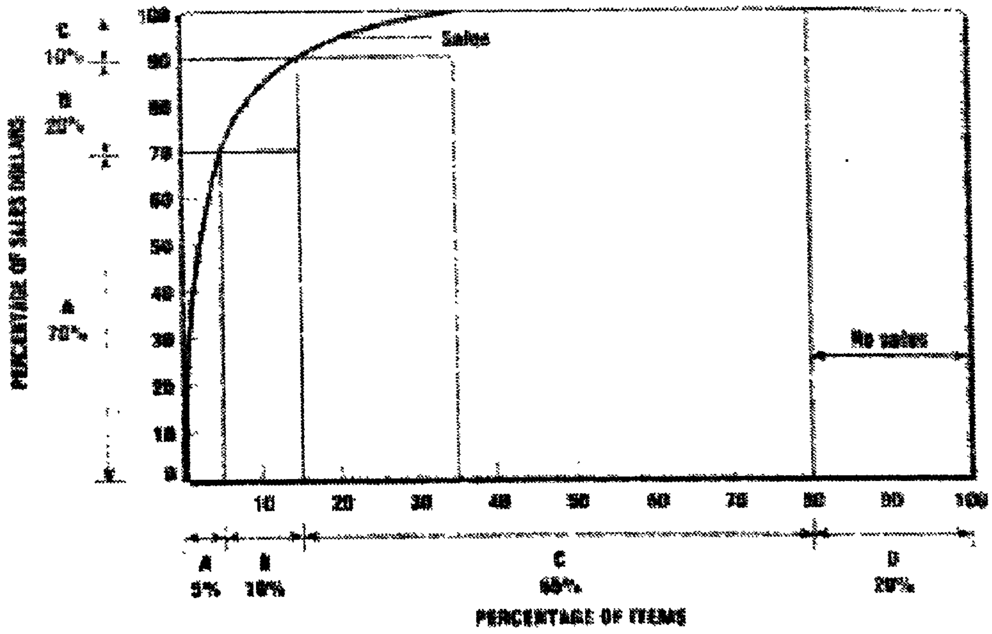
1.ABC Analysis

ABC analysis utilizes the 80: 20 principle, which implies that 80 % of the sales come from 20 % of the products.

The first step in the ABC analysis' is to rank order SKUs, using one or more criteria. The most important performance measure for this type of analysis is **Contribution margin,** where:

Contribution margin = Net sales - Cost of goods sold - Other variable expenses

Other variable expenses can include: sales commissions. Sales can be the sales per square foot, the gross margin or the GMROI.



The next step *is* to determine how items with different levels of profit or volume, should be, treated. The buyer may define as category A, those items that account for 5% of the total quantity of items but represent 70% of the sales. Category B items usually represent 10% of the quantity and 20% of the sales. Category C items usually account for 65% of the SKUs, but contribute only 10% of the sales whereas category D consists of those items for which there were no sales in the past season.

2. Sell Through Analysis

A sell through analysis is a comparison between the actual and the planned sales, to determine as to whether early markdowns are required or whether more merchandise is needed to satisfy demand. There is no rule, which can determine when a mark down *is* necessary. It depends on factors like the past experience with the merchandise whether the merchandise is scheduled to be featured in advertising, whether the vendor can reduce the buyer's risk by providing markdown money, etc.

If actual sales stay significantly ahead of the planned sales, a reorder should be made.

3. Multiple Attribute Method

This method uses a weighted average score for each vendor. The following steps are followed:

(a) Develop a list of issues to consider for decision-making-vendor reputation, service, merchandise quality, selling history, etc.

(b) Give importance weights to each attribute.

(c) Make judgments about each individual brand's performance on each issue.

(d) Combine the importance and performances

(e) Add all to arrive at the brand score

The Multiple Attribute Method can evaluate by using the ABC analysis, the Sell Through Analysis or merchandise performance. The Gross Margin Return on Investment or GMROI is a useful tool for merchandise planning. It can help identify products, which are winners and those that need attention. Other methods of managing inventory investments include predetermining the Reorder Point and by determining the Economic Order Quantity.

6.11 Summary

Merchandise budgeting follows a step by step process, open to buy system provides decision on the amount which the buyer has left to spend on a given time period and analyzing of the performance of particular merchandise is most important to take future decisions related to those goods. Tools available to analyze merchandise performance are ABC analysis, the sell through analysis and the multiple attribute method.

Check Your Progress Questions

1.What are the elements of merchandise budgeting?
2.What is the formula for open to buy?
3. What do you mean by open to buy?
4.What are the tools available to measure performance of merchandise?

6.12 Answer to 'Check Your Progress' Questions

1.The elements of merchandise budget are Planned monthly sales, Planned beginning-of-month (BOM) stock, Monthly retail reductions, Planned end-of-month (EOM) stock , Planned purchases for the month at retail price , Planned purchases for the month at cost , Initial markup for the month and Planned gross margin for the month .
2.The formula for open to buy is : Open-to-buy (at retail) = Planned purchases - Purchase commitments

3. Open-to-buy is the amount the buyer has left to spend for a given time period, typically a month.

4.Tools available to analyze merchandise performance are ABC analysis, the sell through analysis and the multiple attribute method.

6.13 Exercise and Questions

1.What are the steps involved in merchandise budgeting?

2.How will you calculate open to buy for past and present periods – Illustrate.

3.What are the tools available for analyzing merchandise performance – elaborate.

6.14 Further Readings

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985

Unit – 7

Structure:

7.0 Introduction
7.1Unit Objectives
7.2 Brand Strategies
7.3 Brand Associations and Awareness
7.4 Manufacturer Brands
7.5Private brands pros and cons
7.6 Private brand Options
7.7 International Sourcing Decisions – Cost and Managerial issues
7.8 Summary
7.9 Answers to 'Check Your Progress' Questions
7.10 Exercises and Questions
7.11 Further Readings

7.0 Introduction

Branding is an inevitable part of retail merchandising where the retailer have to create high level of awareness, develop favorable associations with the brand name and consistently reinforce it. Another important thing is that whether the retailer is going to deal with manufacturers brand or his own private label. In several cases retailers source products from across borders for which several cost and management implications are to be considered. An elaborate discussion is made on the above in this chapter.

7.1Unit Objectives

- Understanding importance of brand strategy
- Discussing pros and cons of private and manufacturer brands
- Understanding cost and managerial implications of international sourcing decisions

7.2 Branding Strategies:

A brand is a distinguishing' name or symbol, such as a logo, that identifies the products or services offered by a seller and differentiates those products and services from the offerings of competitors. In a retailing context, the name of the Retailer is a brand that indicates to consumers the type of merchandise and services offered by the retailer .Some retailers develop a private-label or store brand that are exclusively sold through their channels. In some cases, this private-label merchandise bears the retailer's name.

Value of Brand Image

Brands provide value to both customers and retailers. Brands convey information to consumers about the nature of the shopping experience- the retailer's mix -they will encounter when patronizing a retailer. They also affect the customers' confidence In decisions made to buy merchandise from a retailer. Finally, brands can enhance the customers' satisfaction with the merchandise and services they buy.

The value that brand image offers retailers is referred to as brand equity. Strong brand names can affect the customer's decision-making process, motivate repeat visits and purchases and build loyalty. In addition, strong brand names enable retailers to charge higher prices and lower their marketing costs. Customer loyalty to brands arises from heightened awareness of the brand and the emotional ties towards it. A Strong brand image enables retailers to increase their margins. When retailers have high customer loyalty, they can engage in premium pricing and reduce their reliance on price promotions to attract customers. Brands with weaker images are forced to offer low prices and frequent sales to maintain their market share. Finally, retailers with strong brand names can leverage their brand to successfully introduce new retail concepts with only a limited amount of marketing effort.

Building Brand Equity

The activities that a retailer needs to undertake to build the brand equity for its firm or its private-label merchandise are
(1) create a high level of brand awareness,
(2) develop favorable associations with the brand name, and
(3) consistently reinforce the image of the brand.

7.3 Brand Awareness

Brand awareness is the ability of a potential customer to recognize or recall that the brand name is a type of retailer or product/service. Thus, brand awareness is the strength of the link between the brand name and type of merchandise or service in the minds of customers. There is a range of awareness from aided recall to top-of-mind awareness.

Aided recall is when consumers indicate they know the brand when the name is presented to them.

Top of- mind awareness, the highest level of awareness, arises when consumers mention a brand name first when they are asked about the type of retailer, a merchandise category, or a type of service.

Associations

Building awareness is the first step in developing brand equity the value of the brand is largely based on the associations that customers make with the brand name. Brand associations are anything linked to or connected with the brand name in a consumer's memory. For example, some of the associations that consumers might have with McDonald's are golden arches,food, clean stores, hamburgers, French fries, Big Mac, and Ronald McDonald.

Some common associations that retailers develop with their brand name are

1. *Merchandise category.* The most common association is to link the retailer to a category of merchandise.

2. *Price/quality.* Some retailers, want to be associated with offering high prices unique and high fashion merchandise. Other retailers want associations with offering low prices and good quality product.

3. *Specific attribute or benefit.* Retailer can link its stores to attributes such as convenience or service.

4. *Life style or activity.* Some retailers associate their name with a specific lifestyle or activity. For example, The Nature Company, a retailer offering books and equipment to study nature, is linked to a lifestyle of interacting with the environment. Electronic Boutique is associated with home use of computer game software.

The brand image is a set of associations that are usually organized around some meaningful themes. Thus, the associations that a consumer might have about Mc-Donald's might be organized into groups such as kids, service, and type of food.

7.4 Manufacturer's Brands

A retailer may decide that he wants to stock a particular manufacturer's brands in his store. Manufacturers' brands are brands for which the manufacturer is responsible in terms of having to develop the merchandise and to establish an image for the brand. These brands are often referred to as national brands

A manufacturer may use the company name as a part of the brand name. Alternately, he may develop separate brand names for each product and may not associate them with the name of the company. Products like Kellogg's cornflakes, Arrow, Lee, Levi's, Samsung, Sony, Phillips and Bata are all examples of manufacturer's brands. Many a times, retailers organize the buying around their most important national brands. For instance, buyers in departmental stores may be responsible for brands such as Lakme, Paco, Estee,Lauder, rather than for lipsticks and fragrances. Retailing manufacturer's brands may help the store image, may increase the traffic flow and may reduce the selling promotional expenses.

Licensing is an arrangement whereby, the owner (licensor) of a particular image or design sells the right to use the image or design to another party, typically, a manufacturer (licensor). The licensee may be either.

- A retailer who contracts with a manufacturer, to produce the licensed product, or A third party who contracts to have the merchandise produced and then, sells it to the retailer.

An example of a licensed product could be sunglasses manufactured by Bausch & Lomb with the Donna Karan label on them.

The different types of licensing are:

1. **Character Licensing** This includes cartoon characters, movie characters and fictional images. Examples include cartoon characters like Disney characters, Peanuts, Barbie Doll, Superman, etc.

2. **Corporate Licensing** This includes brand names and trademarks of corporations, such as IBM, Coca-Cola.

3. **Designer Name Licensing** This is the type of licensing used by designers such as Pierre Cardin, YSL, Ralph Lauren, Donna Karan, etc. These designers lend their names to products not necessarily manufactured or designed by them.

4. **Celebrity Name Licensing** In this case, celebrities license their names to various products. Examples include Stephanie Powers, who has licensed her name to Sears. Closer home, an example of such licensing may be the various brands of perfumes licensed by celebrities like Lata Mangeshkar, Zeenat Aman, etc.

5. **Nostalgia Licensing** This form of licensing includes licensing of the names of legends such as Marilyn Monroe, Lady Diana, etc '

7.5 Private-Label Brands

Private-label brands, also called store brands, are products developed by a retailer and available for sale only from that retailer. Typically, retail buyers or category managers develop specifications for the merchandise and then contract with a vendor to manufacture it. But the retailer, not the manufacturer, is responsible for promoting the brand. Retailers' use of private labels was relatively small in the past for several reasons.

First, national brands had been heavily advertised on TV and other media for decades, creating a strong consumer franchise.

Second, *it had been hard for retailers to gain the economies of scale in design and* production necessary to compete against manufacturer brands.

Third, many retailers weren't sophisticated enough to aggressively compete against manufacturer brands.

Finally, private labels had a reputation of being inferior to manufacturer brands.

In recent years as the size of retail firms has increased through consolidation, private labels have assumed a new level of significance by establishing distinctive identities among retailers. Some retailers, such as The Gap and The Limited, sell their own labels exclusively as an internal element of their distinctiveness.

Other retailers, such as JC Penney and Sears, successfully mix manufacturer brands with their own retailer brands to project their unique image statement .
Offering private labels provides a number of benefits to retailers:

First, the exclusivity of strong private labels boosts store loyalty.

Second, advantage of buying from private-label vendors is that they can enhance store image if the brands are of high quality and fashionable.

Third, like manufacturer brands, successful private-label brands can draw customers to the store. They can be a good deal-10 to 18 percent less expensive than national Brands.

Fourth, retailers that purchase private-label brands don't have the same restrictions on display, promotion, or price that often encumber their strategy with manufacturer brands. Retailers purchasing private brands also have more control over manufacturing, quality control, and distribution of the merchandise.

Finally, gross margin opportunities may be greatest.

Drawbacks of using private-label brands

Although gross margins may be higher for private-label brands than for manufacturer brands, there are other expenses that aren't readily apparent. Retailers must make significant investments to design merchandise, create customer awareness, and develop a favorable image for their private-label brand. When private-label vendors are located outside the home country complications become even more significant, as well Sales associates may need additional training to help them sell private-label brands against better-known brands. If the private label merchandise doesn't sell, the retailer can't return the merchandise to the vendor. These problems are most severe for high-fashion merchandise.

7.6 Private-Label Options

Retail branding strategies have run the gamut from closely imitating manufacturer-brand packaging and products to distinct brand images, from low product quality and prices to premium positioning, and from nonexistent promotion and merchandising to intense activity. We group private brands into four broad categories: copycat, bargain, premium, and parallel.

Bargain branding:

Targets a price-sensitive segment by offering a no-frills product at a discount price known as generic or house brands, such unbranded, unadvertised merchandise is found mainly in drug, grocery, and discount stores. The bargain brand, frequently referred to as the house brand, generally is perceived by the consumer to be of lower quality, and its packaging identifies it as a brand of the retailer. In the context of differentiating the retailer, bargain branding is primarily defensive, Its value comes from

neutralizing competitors who may gain an advantage from discount pricing and by serving a secondary market segment whose patronage potentially leads to collateral sales.

Premium branding:

It offers the consumer a private label at a comparable manufacturer-brand quality, usually with modest price .The premium brand attempts to match or exceed the product quality standards of the prototypical manufacturer brand in its category. There is no intention to duplicate the packaging or to trade off the brand equity of a particular manufacturer brand. However, consumers frequently perceive the retailer premium labels as competing manufacturer brands.

Retailer premium brands, with the appearance of comparability, compete directly with manufacturer national brands. To succeed, the retailer must commit the resources in market research, product development, quality control and promotion in its market area commensurate with its manufacturer-brand competitors. Consequently, development of a premium-branding program precludes many retailers that have few resources from diverting to this strategy.

Copycat branding

It imitates the manufacturer brand in appearance and packaging, generally is perceived to be of lower quality, and is offered at a lower price. For example, copycat brands abound in the fragrance market. By not drawing attention to the brand's origin, the copycat can confuse the consumer about the source of the product. Copycat branding is a risky private-branding alternative because close copies can violate packaging and patent laws. Poor copies are ineffective.

Parallel branding

Private labels that closely imitate the packaging and product attributes of leading manufacturer brands but with a clearly articulated "invitation to compare" in its merchandising approach and on its product label. This invitation to compare on the product label was the basis for a recent legal action. Like copycat branding, parallel branding seeks to benefit from the brand equity of the manufacturer brand by closely imitating the national brand's packaging and product qualities. However, the invitation to compare leaves little doubt that different manufacturers produce the two products. Consequently, the imitative packaging does not constitute a trademark infringement. Nevertheless, patent considerations can be an issue if appropriate discretion is not used.

Parallel branding is a leveraging strategy used to bolster a retailer's private brand sales. The closer two products are in form, logo, labeling, and packaging, the more they are perceived as substitutes. Parallel brands attempt to produce a product and packaging similar to the manufacturer brand that the only noticeable difference between the two is price. This promotes the view that the parallel brand provides better value for the consumer. Manufacturer brands produce store traffic, and the parallel brand leverages this traffic into parallel brand sales through similar packaging and aggressive store signage, displays and shelf location.

7.7 INTERNATIONAL SOURCING DECISIONS

Although retailers buying manufacturer brands usually aren't responsible for determining where the merchandise is made, a product's country of origin is often used as a signal of quality. Certain items are strongly associated with specific countries, and products from those countries, such as gold jewelry from Italy or cars from Japan, often benefit from those linkages.

Superficially, it often looks like retailers can get merchandise from foreign suppliers cheaper than from domestic sources. Unfortunately, there are a lot of hidden costs, including managerial issues, associated with sourcing globally.

sources of supply:

The prime reasons for looking at international sourcing could be the uniqueness

of the merchandise, or the unavailability of the merchandise in the domestic market. Low cost and good quality are also factors which could affect this decision. On the other hand, a retailer may also source from a foreign market simply because the merchandise is unique and because certain customers are always looking for a unique product.

A decision that is closely associated with the branding decisions is to determine where the merchandise is made. Although retailers buying manufacturer's brands, usually aren't responsible for, determining where the merchandise is made, a product's country of origin is often seen as a sign of quality.

In order to source goods, from the international market. The retailers may use the facilities of the Resident Buying Offices that it may have. For example. a large number of international retailers have their buying offices in India. The resident buying offices not only have an understanding of the local market, but once the orders are placed, the offices can-make out the contracts, follow up on the delivery and on the quality control. Alternately, trade shows and wholesale market centers in various cities of the world provide a good opportunity for the buyers and sellers to meet.

Costs Associated with Global Sourcing Decisions

A demonstrable reason for sourcing globally rather than domestically is to save money. Retailers must examine several cost issues when making these decisions. The cost issues discussed in this chapter are country-of-origin effects. Foreign currency fluctuations, tariffs, free trade zones, inventory carrying costs, and transportation costs.

Country-of-Origin Effects The next time you're buying a shirt made in Western Europe (e.g., Italy, France, or Germany), notice that it's probably more expensive than a comparable shirt made in a developing country like Hungary, Ecuador, or Cambodia. These Western European countries have a reputation for high fashion and quality. When making international sourcing decisions, therefore, retailers must weigh the savings associated with buying from developing countries with the panache associated with

buying merchandise from a country that has a reputation for fashion and quality. Other countries might have a technological advantage in the production of certain types of merchandise and can therefore provide their products to the world market at a relatively low price. For example. Japan has always been a leader in the development of consumer electronics. Although these products often enter the market at a high price, the price soon drops as manufacturers learn to produce the merchandise more efficiently.

Foreign Currency Fluctuations An important consideration when making global sourcing decisions is fluctuations in the currency of the exporting firm. Unless currencies are closely linked, for example, between the United States and India changes in the exchange rate will increase or reduce the cost of the merchandise.

Tariffs A tariff, also known as a duty, is a tax placed by a government on imports. Import tariffs have been used to shield domestic manufacturers from foreign competition and to raise money for the government. In general. since tariffs raise the cost of imported merchandise. Retailers have always had a strong incentive to reduce them. The General Agreement on Tariffs and Trade (GATT), and foreign trade zones all reduce tariffs.

World Trade Organization The World Trade Organization *(WTO)* replaced GATT in 1996. With 144 member-countries, the WTO has become the global watchdog for free trade. As a result of the WTO and its predecessor GATT, worldwide tariffs have been reduced from 40 percent in 1947 to an estimated 4 percent in 2000.WTO will continue to push for tariff reductions on manufactured goods as well as liberalization of trade in agriculture and services.

Free Trade Zones Retailers involved in foreign sourcing of merchandise can lower import tariffs by using free trade zones. A free trade zone is a special area within a country that can be used for warehousing, packaging, inspection, labeling, exhibition, assembly, fabrication, or transhipment of imports without being subject to that country's tariffs.

To illustrate how a free trade zone can benefit retailers, consider how German cars are imported to a foreign trade zone in Guatemala for distribution throughout Central America. The duty for passenger vehicles is 100 percent of the landed cost of the vehicle. The duty for commercial vehicles, however is *only* 10 percent. The German manufacturer imported commercial vans with no seats or carpeting, and with panels instead of windows. After paying the 10 percent import duty, it converted the vans to passenger station wagons in the free trade zone in Guatemala and sold them throughout Latin America.

Inventory Carrying Cost The cost of carrying inventory is likely to be higher when purchasing from suppliers outside the United States than from domestic suppliers.
Cost of carrying inventory = Average inventory value (at cost) X Opportunity cost of capital .

The opportunity cost of capital is the rate available on the next best use of the capital invested in the project at hand. It would include the cost of borrowing money for a similar investment, plus insurance and taxes. There are several reasons for the higher inventory carrying costs. Consider The Spoke bicycle store in Aspen, Colorado, which is buying Motor bicycles manufactured in Steamboat Springs, Colorado.

The Spoke knows that the lead time-the amount of time between recognition that an order needs to be placed and the point at which the merchandise arrives in the store and is ready for sale-is usually two weeks, plus or minus three days. But if The Spoke is ordering bikes from Italy, the *lead* time might be three months, plus or minus three weeks. Since lead times are longer, retailers must maintain larger inventories to ensure that merchandise is available when the customer wants it, Larger inventories mean larger inventory carrying costs.

It's also more difficult to predict exactly how long the lead time will be when sourcing globally. When the bicycle goes from Steamboat Springs to Aspen, the worst

that could happen is getting caught in a snowstorm for a day or two. On the other hand, the bicycle from Italy might be significantly delayed because of multiple handlings at sea or airports, customs, strikes of carriers, poor weather, or bureaucratic problems. Similar to long lead times, inconsistent lead times require the retailer to maintain high levels of backup stock.

Transportation Costs In general, the farther merchandise has to travel, the higher the transportation cost will be for any particular mode of transportation, For instance, the cost of shipping a container of merchandise by ship from China to New York is significantly higher than the cost from Panama to New York.

Managerial Issues Associated with Global Sourcing Decisions

In the previous section, we examined the specific costs associated with global sourcing decisions. In most cases, retailers can obtain hard cost information that will help them make their global sourcing decisions. The managerial issues discussed in this section-are quality control and developing strategic partnerships are not as easily evaluated.

Quality Control When sourcing globally, it's harder to maintain and measure quality standards than when sourcing domestically. Typically, these problems are more pronounced in countries that are far away and underdeveloped. For instance, its easier to address a quality problem if it occurs on a shipment of dresses from Costa Rica to the United States than if the dresses were shipped from India because Costa Rica is much closer, There are both direct and indirect ramifications for retailers if merchandise is delayed because it has to be remade due to poor quality. Suppose Tibre is having pants made in Coimbatore. Before the pants leave the factory, Tibre representatives find that the workmanship is so poor that the pants need to be remade. This delay reverberates throughout the system. Tibres outlet could have extra backup stock to carry it through until the pants can be remade, More likely, however, it won't have advance warning of the problem, so the stores will be out of stock. A more serious problem occurs if the pants are delivered to the stores without the problem having been detected. This could happen if the defect is subtle, such as inaccurate sizing. Customers can become irritated and

question merchandise quality. Also, markdowns ensue because inventories become unbalanced and shopworn.

Building Strategic Partnerships The importance of building strategic partnerships is,It is typically harder to build these alliances when sourcing globally. Particularly ,when the suppliers are far away and in underdeveloped countries. Communications are more difficult. There is often " language barrier and there are almost always cultural differences. Business practices-everything from terms of payment' to the modes of trade Such a location enables the buyer to understand the trends in the market and evaluate the new practices such as commercial bribery are different in a global setting. The most important element in building a strategic alliance and maintaining the supplier's trust is more arduous in an international environment. More will be discussed about Strategic Alliances in Unit 8.

7.8 Summary

Brands provide value to retailers, the decision on handling manufacturer brands vs private labels carries its own pros and cons. The strategic vision of the retailer provides basis for the decision related to the choice of branding strategy. International sourcing decisions carries with it several managerial implications and cost constraints but still its deemed inevitable in the highly globalized era.

Check Your Progress Questions

1.What do you mean by brand awareness?

2. Give note on Manufacturer brand and Private brand.

3. What are the steps involved in building brand equity?

4.What are the associations made by retailers to a brand?

7.9 Answers to 'Check Your Progress' Questions

1.Brand awareness is the ability of a potential customer to recognize or recall that the brand name is a type of retailer or product/service.

2. Private-label brands, also called store brands, are products developed by a retailer and available for sale only from that retailer and Manufacturers' brands are brands for which the manufacturer is responsible in terms of having to develop the merchandise and to establish an image for the brand.

3. The activities that a retailer needs to undertake to build the brand equity for its firm or its private-label merchandise are

(1) Create a high level of brand awareness,

(2) Develop favorable associations with the brand name, and

(3) Consistently reinforce the image of the brand.

4. Some common associations that a retailer develop with their brand name are: Merchandise category, Price/Quality, Specific attribute and Lifestyle or activity.

7.10 Exercise and Questions

1.Assume your self as a private lable retailer and enumerate on your brand building strategy giving examples.

2.What are the cost and managerial implications related to international sourcing decisions?

3. Discus the pros and cons of Private vs Manufacturer brands.

7.11 Further Readings

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985

Unit – 8

Structure:

8.0 Introduction
8.1Unit Objectives
8.2 Merchandise buying process
8.3 Guidelines for negotiating with vendors
8.4 In-store merchandise handling
8.5 Building strategic relationships
8.6 Maintaining strategic relationships
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8.0 Introduction

The basic role of a buyer is to find, evaluate and select merchandise for the retail store. For this purpose he needs to answer what, when, how much, where and from whom to buy the goods. This chapter focuses on the buying technique which can be used by a buyer to determine his source of supply , an elaborate note is given on the guidelines for negotiating and building long term strategic partnership with vendors.

8.1UnitObjectives

- Understanding merchandise buying process
- Learning consideration areas of vendor negotiation
- Discussing on building and maintaining strategic relationship with vendors
- Learning legal issues related to merchandising

8.2 Merchandise Buying Process

Stage 1 Locating Sources

Domestic sources of supply may be located by visiting central markets, trade shows or expositions. Usually, each city has its own central market, where a large number of key suppliers are located.

Stage 2 Analyzing Vendors

A decision needs to be taken on the potential vendors.

The following criteria need to be kept in mind:

1. The target market for which the merchandise is being purchased.
2. The image of the retail organization and the fit between the product and the image of the retail organization.
3. The merchandise and prices offered.
4. Terms and services offered by the vendor.
5. The vendor's reputation and reliability.

The retail buyer then needs to negotiate on the price, the delivery dates, the discounts, the shipping terms and the possibilities of returns. While negotiating with the vendors, it is necessary to keep in mind their history, their goals and constraints. At the same time, the buyer needs to be aware of the real deadlines and work towards fulfilling them.

The following are the types of discounts that could be available to the buyer:

1. **Trade Discounts** These are reductions in the manufacturer's suggested retail price,
2. **Chain Discounts** This is the traditional manner of discounting, where a number of different discounts are taken sequentially, from the suggested retail price (e.g. 50 – 10)

3.Quantity Discounts These can be cumulative and, non-cumulative. Retailers earn quantity discounts by purchasing certain quantities over a specified period of time.

4.Seasonal Discount This is an additional discount offered as an incentive to retailers to order merchandise in advance of the normal buying season.

5.Cash Discount It is the reduction in the invoice cost for paying the invoice, prior to the end of the discount period.

Each retailer will have his own criteria for the selection of vendors. The starting point may be a vendor registration form, which provides the details on address, the preferred mode of payment, the sales tax number, etc. Registration with the relevant tax authorities, e.g. for Sales Tax, is a basic criteria used by many retailers to eliminate suppliers.

Stage 3 Establishing Relationships with Vendors

Retailers have for long, been wary of sharing information with their suppliers. This is hardly surprising--considering their traditionally competitive relationship, with both sides trying to get best of every deal. However, times have changed, and many retail organizations work with their suppliers as a team, to create a competitive advantage.

Stage 4 Analyzing Vendors Performance

In case a buyer is dealing with multiple vendors for a particular product category, he can draw conclusions on a vendors' performance by listing out the following:

- The total orders placed on the vendor in a year,
- The total returns to the vendor, the quality of the merchandise,
- The initial markup on the products,
- The markdown, if any,
- Participation of the vendor in various schemes and promotions,
- Transportation expenses, if borne by the retailer.

- Cash discounts offered by the vendor, and lastly,
- The sales performance of the merchandise.

A factual evaluation of the vendors helps the buyers in being unbiased and in taking the right decisions for the retail organization. Respect and co-operation between the buyers and the vendors is necessary to build long-term relationships. In the fast changing world of retail, it is also necessary to share information with the vendors on a timely basis, so as to avoid stock outs or situations requiring heavy markdowns.

8.3 Negotiating With Vendors.

Negotiations are as basic to human nature as eating or sleeping. A negotiation takes place any time two parties confer with each other to settle some matter. Negotiations take place between parents and their children about issues like allowances. People negotiate with their friends about what to do on the weekend. People negotiate for higher salaries, better offices, and bigger budgets negotiations are crucial in buyers discussions with vendors. No one should go into negotiation without intensive planning

Guidelines for Planning Negotiations with Vendor

KNOWEDGE IS POWER The more the buyer knows about the vendor, the better his negotiating strategy will be.

Consider History Buyers need a sense of what has occurred between the retailer and vendor in the past. An established vendor may be more likely to take care of old problems and accept new demands if a long-term, profitable relationship already exist.

Assess Where Things Are Today some vendors believe that once they've sold merchandise to the retailer, their responsibility ends. This is a short-term perspective, however, If the merchandise doesn't sell, a good vendor, will arrange to share the risk of loss.

Set Goals Besides taking care of last season's leftover merchandise, the buyer for the upcoming meeting: additional markup opportunities, terms of purchase, transportation, delivery and exclusivity, communications, and advertising allowances.

Additional Markup Opportunities Vendors may have excess stock (manufacturers' overruns) due to order cancellations, returned merchandise from retailers, or simply an overly optimistic sales forecast. To move this merchandise, vendors offer it to retailers at lower than normal prices. Retailers can then make a higher than normal gross margin or pass the savings on to the customers.

Terms of Purchase It's advantageous for buyers to negotiate for a long time period in which to pay for merchandise. Long terms of payment improve the firm's cash flow position, lower its liabilities (accounts payable), and can cut its interest expense if it's borrowing money from financial institutions to pay for its inventory.

Transportation Transportation costs can be substantial; nonetheless, the question of who pays for shipping merchandise from vendor to retailer can be a significant negotiating point.

Delivery and Exclusivity In retailing in general , and in fashion in particular, timely delivery is essential. Being the only retailer in a market to carry certain products helps a retailer hold a fashion lead and achieve a differential advantage.

Communications Vendors and their representatives are excellent sources of market information. They generally know what is and isn't selling. Providing good, timely information about the market is an indispensable and inexpensive marketing research tool.

Advertising Allowances Retailers have the choice of advertising any product in the store. They can sometimes share the cost of advertising through a cooperative arrangement with vendors known as co-op advertising-a program undertaken by a vendor

in which the vendor agrees to pay all or part of a pricing promotion. By giving retailers advertising money based on a percentage of purchases, vendors can better represent their product to consumers.

Know the Vendor's Goals and Constraints Negotiation can't succeed in the long run unless both parties believe they've won. Generally, vendors are interested in providing a continuous relationship, testing new Items, facilitating good communications, and providing a showcase to feature their merchandise.

Continuous Relationship Vendors want to make a long-term investment in their retailers. For seasonal merchandise like men's designer shirts, they have to plan their production in advance so it's important to ensure long term relationship with outlets this has to be favored by the outlet management.

Testing New Items There's no better way to test how well a new product will sell than to put it in a store. Retailers are often cautious with new items due to the risk of markdowns and the opportunity cost of not purchasing other, more successful merchandise. Yet vendors need their retailers to provide sales feedback for new items.

Communication about the market demand can be passed on to the manufacturer which will be more beneficial to them.

8.4 In-Store Merchandise Handling

The retailer will need to have some means of handling incoming merchandise. For some types of retailers (e.g., a grocery store), this need will be significant and frequent; for others (e.g., a jeweler), it will be relatively minor and infrequent. A retailer with a

frequent and significant amount of incoming merchandise needs considerable planning of merchandise receiving and handling space.

To illustrate, consider that a full line grocery store will need to build receiving docks to which 40-to-60-foot semi trailers can be backed up. Similarly, space may be needed for a small forklift to drive between the truck and the merchandise receiving area to unload the merchandise. Subsequently, the merchandise will need to be moved from the receiving area, where it will be counted and marked, to a storage area, either on the selling floor or in a separate location.

The point at which incoming merchandise is received can be a high-theft point. The retail manager needs to design the receiving and handling area in order to minimize this problem. Several types of theft will be mentioned in the following discussion. Some involve, the retail employees themselves, others involve outsiders.

Vendor collusion includes the types of losses that occur when the merchandise is delivered. Typical losses involve the delivery of less merchandise than is charged for, removal *'of* good merchandise disguised as old or stale merchandise, and stealing other 'merchandise from the stockroom or off the selling floor while making delivery. This type of theft often involves both the delivery people and the retail employee who signs for the delivery with the two splitting the profit.

Employee theft occurs when employees steal merchandise where they work. Although no one knows for sure how much is stolen annually from retailers, because all shrinkage statistics are based only on apprehensions, as many as 30 percent of American workers admit to stealing from their employers, even if it is only small items like a pen or pencil. Although some of the stolen goods come from the selling floor, a larger percentage is taken from the stockroom to the employee lounge and lockers, where it is kept until the employees leave with it at quitting time. Employee theft, is most prevalent in food stores, department stores, and discount stores. Considering that these types of stores are usually

larger in size, sales volume, and number of employees, the lack of close supervision might contribute to this problem.

8.5 Building Partnering Relationships

Although not all retailer vendor relationships should or do become strategic partnerships, the development of strategic partnerships tends to go through a series of phases characterized by increasing levels of commitment: (1) awareness, (2) exploration, (3) expansion, and (4) commitment.

In the **awareness stage**, no transactions have taken place. This phase might begin with the buyer seeing some interesting merchandise at a retail market or an ad in a trade magazine. Reputation and image of the vendor can play an important role in determining if the buyer moves to the next stage.

During the **exploration phase**, the buyer and vendor begin to explore the potential benefits and costs. At this point, the buyer may make a small purchase and try to test the demand for the merchandise in several stores. In addition, the buyer will get information about how easy it is to work with the vendor.

Eventually, the buyer has collected enough information about the vendor to consider developing a longer-term relationship. The buyer and the vendor determine that there is a potential for a win-win relationship. They begin to work on joint promotional programs, and the amount of merchandise sold increases.

If both parties continue to find the relationship mutually beneficial, it moves to the commitment stage and becomes a strategic relationship. The buyer and vendor make significant investments in the relationship and develop a long-term perspective toward it.

It is difficult for retailer-vendor relationships to be as committed as some supplier-manufacturer relationships. Manufacturers can enter into monogamous (sole source) relationships with other manufacturers. However, an important function of retailers is to provide an assortment of merchandise for Thus, they must always deal with multiple, sometimes competing Suppliers.

8.6 MAINTAINING STRATEGIC RELATIONSHIPS

Relationships between retailers and vendors are often based on arguing over'-splitting up a profit pie This is basically a win-lose relationship because when one party gets a larger portion of the pie, the other parry gets a smaller portion. Both parties are interested exclusively in their own profits and are unconcerned about the other party's welfare, these relationships are common when the products are commodities and have no major impact on the retailers' performance. Thus, there is no benefit to the retailer to enter into a strategic relationship.

A strategic relationship, also called a partnering relationship, is when a retailer and vendor are committed to maintaining the relationship over the long term and investing in opportunities that are mutually beneficial to the parties, In these relationships, it's important for the partners to put their money where their mouth is. They've taken risks to expand the pie to give the relationship a strategic advantage over other companies.

Thus, a strategic relationship is a win-win relationship, Both parties benefit because the size of the pie has increased-both the retailer and vendor increase their sales and profits, Strategic relationships are created explicitly to uncover and exploit joint opportunities, Members in strategic relationships depend on and trust each other heavily; they share goals and agree on how to accomplish those goals; and they're willing to take risks, share confidential information, and make significant investments for the sake of the relationship.

Maintaining Strategic Relationships

Four foundations of successful strategic relationships are mutual trust, open communication, common goals, and credible commitments.

Mutual Trust The glue in strategic relationship is trust. Trust is a belief that a partner is honest (reliable, stands by its word, sincere, fulfills obligations) and is benevolent (concerned about the other party's welfare)When vendors and buyers trust each other, they're more willing to share relevant ideas, clarify goals and problems, and communicate efficiently.

Open Communication In order to share information, develop sales forecasts together, and coordinate deliveries, Wal-Mart and P&G have to have open and honest communication. This may sound easy in principle, but most businesses don't like to share information with their business partners. They believe it is none of the other's business. But open, honest communication is a key to developing successful relationship. Buyers and vendors in a relationship need to understand what's driving others business.

Common Goals Vendors and buyers must have common goals for a success- relationship to develop. Shared goals give both members of the relationship incentive to pool their strengths and' abilities and to exploit potential opportunities between them. There's also assurance that the other partner won't do anything to hinder goal achievement within the relationship.

Credible Commitments Successful relationships develop because both partners make credible commitments to the relationship. Credible commitments are tangible investments in the relationship. They go beyond just making the hollow statement "I want to be a partner." Credible commitments involve spending money to improve the supplier's products or services provided to the customers.

8.7 Legal and Ethical Issues in Merchandise Buying.

While sourcing merchandise from India, a buyer has to take into consideration, the taxes levied by the Central Government, the state government and the municipal taxes. Sales tax is a tax on the sale of goods. The liability to pay sales tax arises on making a sale of goods. In India, the law for levying sales tax is provided for under the Central Sales Tax Act, 1966. The Such-a location enables the buyer to understand the trends in the market and evaluate the new levies excise duties

Central Government and the rate of tax is uniform for a product, across the country. The buyer also needs to take into consideration, the additions to the cost price that wiil come about due to octroi, which is levied in cities like Mumbai and Kolkata. The Municipal Corporation of Greater Mumbai levies octroi on the invoice value of goods entering the city limits.

Before taking a decision on sourcing internationally, the buyer needs to check whether the product to be sourced falls under the Open General list(OGL), the Restricted list or the Negative list. In case the goods fall under the OGL, a Special import License (SIL) is required. Currently, there are 700 products which are on the restricted list for imports and include, among other things, meat, dairy products, cheese, pulses, alcohol, various types of fabrics and garments and a large number of consumer durables. If the retailer wishes to import products which fall under the SIL, the importer has to pay a premium and this again adds to the cost of the product and at times, largely increases the landed cost of the merchandise.

8.8 Summary

Merchandising buying is a four step process involves Identifying, Evaluating, Establishing relationship and analyzing vendor performance. Building and maintainin strategic partnerships is also a crucial part of merchandise buying process, which also passes through four phases awareness, exploration, expansion and commitment.

Check Your Progress Questions

1.What are the bases of negotiation with vendors?

2.What factors are to be considered in in- store merchandise handling?

3.What are the phases of building vendor relationships?

4.What are the factors deemed important for maintaining vendor relationship?

8.9 Answers to 'Check Your Progress' Questions

1.Terms of purchase, transportation, Delivery, Exclusivity, communication, allowances of advertising etc were the common bases of negotiation with vendors.

2.The factors to be considered in in- store merchandise handling are Vendor collisions and Customer theft.

3.The four phases of building vendor relationship are awareness, exploration, expansion and commitment.

4.The factors deemed important for maintenance of strategic relationship are Mutual trust, Open communication, Common goals and Credible commitments.

8.10 Exercise and Questions

1.Elaborate on the process of merchandise buying process?

2.What are the bases of negotiation with vendors? Typically narrate a negotiation process with a textile manufacturer for your retail outlet.

3.How do we build and maintain strategic relationship with vendors?

4.What are the legal and ethical issues related to merchandising?

8.11 Further Readings

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985

Unit 9

Structure:

9.0 Introduction
9.1Unit objectives
9.2 Elements of Retail Price
9.3 Adjustments to retail price
9.4 Categories of potential pricing objectives
9.5 Pricing policies
9.6 Cost oriented pricing
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9.0 Introduction

Price is the integral part of retail mix, the price of the merchandise mix also communicates the image of the retail store to the customers, various factors like the targeted market, store policies, competition and economic conditions need to be taken into consideration while arriving at the price of a product. This chapter elaborately discuses on various areas of retail pricing like elements to retail pricing, adjustments, various objectives and methods of retail pricing.

9.1Unit Objectives

- Understanding elements and adjustments to retail pricing.
- Understanding the pricing objectives
- Discussing various methods of pricing in retailing

9.2 ELEMENTS OF RETAIL PRICE

In order to arrive at the retail price, one needs to first consider the elements that go into the calculation of the price. The first element to be considered is the Cost of Goods, which is the cost of the merchandise and various other expenses that are involved in the movement of the goods from the manufacturer to the actual store. These expenses may be fixed or Variable. Fixed Expenses are those, which do not vary with the quantity of the sale or business done. Shop rents and head office costs fall into this category. The level of sales directly affects the variable expenses. Merchandise margins and the product mix, however, are variable, and their management can either enhance or destroy profitability. The profit to be earned from the merchandise must be planned before fixing the retail price. The profit figure arrived at, can also be expressed as the mark up percentage as shown below:

Retail Price = Cost + Mark Up, or

Cost = Retail Price - Mark Up and

Mark Up = Retail Price - Cost.

The components of this formula can be expressed in rupee terms or as a percentage. The mark up percentage can be expressed as a percentage of the retail price or as a percentage of the cost price.

Thus, the following formulae would apply:

Mark Up Per cent (Based on Retail Price) = Mark Up in Rupees/Retail Price and,

Mark Up Per cent (Based on Cost) = Mark up in Rupees/Cost.

Let us understand these concepts with the help of the following illustration. Assume that the cost of the merchandise of an item is Rs 200 and the mark up is Rs 150. The mark up percentage based on the retail price would work out to 37.5%.

The retail price has been calculated as 200+150 = 350.

Mark Up percentage on retail = 150/350 = 42.86%

Based on the cost price, the mark up percentage can be calculated as under:

Mark Up percentage on cost = 150/200 = 75%

The mark up thus fixed, is termed as the Initial Mark Up. Rarely are all products sold completely at the fixed price. Reductions in price are often made and could be due to markdowns, employee discounts, customer discount and/or shrinkage..

Markdowns are reductions in the original retail price. Markdowns are discussed in detail later in this chapter, in the section on adjustments to retail prices. Discounts offered to customers and employees who buy the product, also reduce the mark up percentage. Shrinkage includes loss of merchandise due to thefts, or damage/spoiled goods. All these costs reduce the profit margin and hence, must be accounted for.

9.3 ADJUSTMENTS TO RETAIL PRICE

Many a times, retail prices need to be adjusted to meet the conditions prevailing in the market. Adjustments to retail prices can be done by way of markdowns or by way of promotions. Markdowns are a permanent reduction in the price and this step may be taken as a result of slow selling of the product as a part of a systematic strategy. Markdowns are usually done after a determined number of weeks, in order to maintain a desired rate of sales.

Timely markdowns help improve the profitability, increase the turnover and increase the profit. Markdowns may be necessitated due to wrong forecasting, overbuying, faulty selling practices or simply because the product is shop spoiled or the odds and ends of a range are left at the end of a season.

The Mark down percentage is calculated as follows:

Total Mark down/Total sales X 100.

Promotions on the other hand, are a temporary reduction in the price, used to generate additional sales during peak selling periods. Prices may be reduced by a percentage (25 per cent off) or to a lower sale price (Rs 99). High volume items, with a substantial initial markup, are usually selected for promotions.

Promotions, may also include coupons, which may reduce the retail price by an amount or a, percentage. With retail coupons, the retailer absorbs the reductions in the price.

A Comparison of Markups and Markdowns

A mark up is where profit is expressed as a percentage of the costs, as shown below:

(price-Cost)/Cost X 100

Thus, a selling price of Rs 30, with a cost of Rs 20, gives a mark up of 50 per cent.

A markdown is where profit is expressed as a percentage of the sale price and is shown below:

(price-Cost)/Price X 100

Thus, a selling price of Rs 60, with a cost of Rs 24, gives a markdown of 60 per cent. %

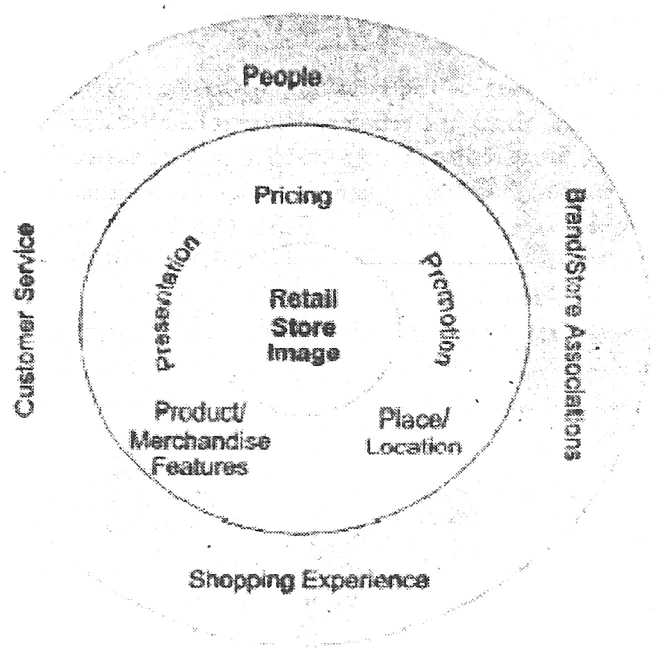
Markdown on selling price = % Mark Up on cost X 100

= 100% + Mark Up on cost %

Mark Up on cost = % Markdown onsellingprice X100

= 100 % - % markdown on selling price

9.4 CATEGORIES OF POTENTIAL PRICING OBJECTIVES



Product Quality Objectives **Product quality objectives** center on recouping costs associated with retail research and development. In addition, product quality objectives can be used in conjunction with IMC tactics to create the perception of high product quality, and thus high retail store quality, in the consumer's mind. This objective is often used together with a skimming objective by high-end retailers.

Example: A retailer prices items at 300 percent above cost to ensure that its prestigious image is firmly established in the consumer's mind.

Skimming Objectives With **skimming objectives** (also called *skimming strategies),* the retailer sets an initial relatively high price for a product. A skimming strategy is often used to recoup costs incurred when selling a new product--costs associated with research, development, and marketing, for instance.

The term *skimming* comes from dairy farms, where personnel skim the high-quality cream from the top of the milk. The cream is more valuable than the milk and can be sold at higher prices. Likewise, the product marketer skims the market with an initial high price to sell to customers who are relatively unconcerned about price. The price may be

lowered later to attract additional customers who are more price conscious. With this strategy, the customer must be somewhat price insensitive and view the product or service as premium quality.

Example: A retailer initially prices a DVD player at $750. After a period of six months, the cost will be lowered to $500. Once competitors enter the market, the price will be set to remain competitive.

Market Penetration Objectives **Market penetration objectives** are the opposite of skimming objectives. Prices are initially set lower to attract large numbers of customers. Market penetration objectives are effective when the retailer's customers are price sensitive. The key to an effective market penetration strategy is to increase sales volumes to offset the low product price. As a general rule, after a certain point, retail costs do not increase very much when sales volume increases. Market penetration objectives have the added benefit of allowing the retailer to discourage competition from entering the trading area because of the lower prices the retailer has already established for the market. In addition, market penetration may help establish a new product as a popular alternative for the consumer, thus creating social pressure to own the product as well as an economic benefit.

Example: A retailer sets prices at lower levels for the first two months of operation to increase market share and discourage competition.

Market Share Objectives **Market share objectives** allow the retailer to adjust price levels based on competitors' changes in price, enabling the retailer to create additional **market share** or reduce market share in relation to the competition. This can be done for the entire retail operation (that is, all stores), for a division, or for a specific store. The retailer can also set a market share objective for each department, product line, or product and brand.

Example: To stand by its "we will not be undersold" policy, a retailer sets its average prices below those of its three main competitors.

Survival Objectives **Survival objectives** allow the retailer to increase price levels to meet sales expenses. This type of objective is generally used to match sales volumes to overall store (or company) expenses.

Example: A retailer sets pricing to cover expenses and increase store profitability over last year's by 5 percent.

Return on Investment (ROI) Objectives Return on investment (ROI) objectives are created to help the retailer meet or exceed stated return on investment figures. Management creates a target return figure it thinks will be satisfactory to stakeholders (primarily stockholders). Then the price is set to reach that targeted return level.

Example: A retailer sets prices to deliver a 15 percent return on investment within one year.

Profit Objectives **Profit objectives** are like ROI objectives, except that target profit levels rather than ROI levels are the goal. If management uses a profit maximization approach to retailing, there is a good chance that profit objectives will be set.

Example: A retailer sets prices to increase profits by 15 percent within one year.

Status Quo Objectives **Status quo objectives** embody the attitude that "Everything is going well-let's not rock the boat." A retailer that wants to stabilize sales will probably utilize a status quo objective.

Example: In the upcoming year, a retailer will price items to match last year's sales.

Cash Flow Objectives **Cash flow objectives** allow the retailer to generate money quickly. These objectives are designed to encourage additional sales volumes. Generally, they are short-term objectives.

Example: During any given month retailer sets prices lower to encourage sales volume and increase cash flow.

Pricing flexibility The range of prices consumers are willing to pay for a particular product or service. There are three steps in determining pricing flexibility.

The first is to determine the costs associated with the retailing operation. Data that will help the retailer determine costs are located in the retailer's financial documents and in the retail information system (RIS).

The second step is to estimate the demand for the products and services, taking the competition into account. The demand estimate helps set the upper price limits for the products. The greater the difference between the upper and lower limits, the more flexible the price is Said to be.

Finally, in the third step, the retailer estimates the elasticity of price for its products and product lines.

9.5 Pricing policies

It help create the overall pricing strategy. Therefore, the retailer must establish general guidelines for price development. Because prices are influential in consumers' perceptions of the quality of the retailer's products. and stores, retailers must pay special attention to pricing tactics and the integration of these tactics into the overall IRM plan. Because product quality and pricing are so interrelated, it is vital that the retailer be consistent when developing and implementing pricing policies. It would be inconsistent for a high-end retailer to offer products and services at discounted prices.

Common factors involved in establishing pricing policies include the need for term profits, competitors' prices, product and supply-chain costs, and historical actions. Several pricing policies are particularly widespread in the retailing industry, including price variability, promotional pricing, price leveling, life cycle pricing, price lining, price stability, and psychological pricing.

PRICE VARIABILITY

Price variability policy (is also known as *differential pricing),* the retailer asks, "Do we want to charge the same price for our product(s) to all our customers, or do we want to charge different prices to different customers?" Although there are some legal restrictions on price variability, retailers have the option to offer the same product to customers at different prices. Sometimes this policy can anger or confuse consumers; thus, an understanding of consumer perceptions is paramount. Price variability used to be referred to as price discrimination, but due to the negative connotation of the term discrimination, it is rarely used today.

PROMOTIONAL PRICING

A retailer coordinates pricing with the promotion variable of IMC. Because the two areas are interrelated, many times the pricing policy becomes tied to promotions. Two main types of promotional pricing are leader pricing (often called *loss leaders)* and special-event pricing.

Leader pricing occurs when products are priced at less than the usual markup, near cost, or below cost. Leader pricing is used to increase traffic. In the process of buying the sale item, the customer typically picks up items at regular prices, thus offsetting the lower revenues from the price leaders.

Special-event pricing, advertised sales are used to generate store traffic. Typically, sales coincide with a major holiday or event, such as Valentine's Day or an inventory clearance.

PRICE LEVELING

Under a **price leveling** policy, the retailer attempts to maintain price levels for the long term. Also called *customary pricing,* this type of policy is typically implemented prior to the actual opening of a retail facility. Retailers use price leveling to communicate to their publics the type of business they are operating. A discount retailer

such as Wal-Mart may choose to set lower prices for all of its products (everyday low pricing, or EDLP), thus supporting its image of a low-price retailer.

When using price leveling, retailers take into account many variables, including the organization's vision and mission statements, corporate culture, and product line objectives; competitors' strengths, weaknesses, and prices; and the state of the economy. The retailer should refer to the situational analysis before setting a price-leveling policy.

LIFE CYCLE-PRICING

Life cycle pricing may be planned based on the product or store life cycle. Under life cycle pricing, price points are set based on the stage of the product life cycle (introduction, growth, maturity, and decline) that the product (or store) has reached. For example, a retailer may use a penetration strategy to enter the market with low prices when it first opens the store. As consumers demand more products (during the growth phase), the retailer raises the prices slightly. As the product reaches maturity, the retailer levels off the price to current market prices. Finally, during the decline phase, the retailer either raises or lowers the price because demand and sales have decreased significantly.

PRICE LINING

A retailer using a price lining policy offers various products and prices to match its competitors' offerings for a particular product category. Price lining is also referred to as the *development of price points.* Therefore, each line of products receives special pricing. This allows the retailer to compete at different levels within a given product line. The goal in a price lining strategy is to maximize profits for the whole line versus focusing on only one product's profitability.

PRICE STABILITY

At times retailers try to create a stable price, or a 'one price policy' for certain products, to avoid price wars with the competition. The popular 'dollar store' formats operate under this price stability policy. These stores do not have to run frequent sales because their customers know prices will remain stable.

PSYCHOLOGICAL PRICING

Because consumers make a correlation between the price of a product and the product's quality, many retailers set prices using psychological pricing. **Psychological pricing** takes into account the consumer's perceptions and beliefs. The three main types of psychological pricing are odd/even pricing, reference pricing, and prestige pricing.

ODD/EVEN PRICING The retailer using **odd/even pricing** places prices on individual products that end in either an odd or an even number. Consumers often perceive the price to be lower if it falls below an expected threshold.

For example, a product that is priced at Rs39.99 is perceived as less expensive than one priced at Rs40.0C. In many cases, consumers expect prices to end in an even number. For example, for products sold from a vending machine, an even price such as Rs 10 is more practical than an odd price such as Rs9.90.

REEFERENCE PRICING. **Reference pricing** uses a consumers' frame of reference to help set price. A frame of reference is established through information searches or previous experience purchasing other like products. Is to uncover customers' expectations, it is important that the retailer survey customers to determine the **just noticeable difference JND).** This is the price at which consumers believe they are paying more or less than the norm or reference price. The key is to find out the magnitude of change necessary for a change in price to be noticed by the consumer.

PRESTIGE PRICING. Selling products at high prices to establish a reputation of quality is called **prestige pricing.** This pricing strategy aims to create "snob appeal"" Manufacturers spend a great deal of time and money developing their brands often sell high-end products to retailers that are associated with prestige. The products demanded by these retailers' customers generally carry a higher, or prestige, price. Think about the last time you shopped for clothes. What stores did you visit? Did you shop at Park avenue rather than Prestige for your jeans? Your decision to shop at either one of those stores shows that you are brand or price sensitive.

9.6 COST-ORIENTED PRICING

To generate a profit, product costs *must* be covered. **Cost-oriented pricing** (also called *cost-plus pricing)* has two approaches: markup pricing (the more common) and breakeven pricing. The retailer needs to determine its markup percentage; one way to do this is to look at traditional product markups within the industry and at the manufacturer's suggested retail price. The retailer must also consider the product's average turnover, the amount of competition for the product, the levels of service required, and the amount of sales time and effort involved in selling the product. All these factors, along with the inclusion of the expected or targeted profit margin, determine the **markup.**

MARKUP PRICING. In markup pricing, two options exist for determining the markup percentage: markup based on the retail, or selling, price of the product, and markup based on the product's cost. The chosen method is generally selected based on the accounting systems the retailer employs.

BREAKEVEN PRICING. Breakeven pricing is the other method used in the creation of a cost-oriented pricing system. With breakeven pricing, the retailer determines the **breakeven point (BEP),** or the level of sales needed to cover all the costs associated with selling the product. The breakeven point is calculated using the following formula:

BEP (in quantity) = Fixed cost/Unit price - Unit variable cost

This formula can be modified to calculate the BEP in value by multiplying the BEP (in quantity) by the selling price of the item.

9.7 COMPETITION-ORIENTED PRICING

In competition-oriented pricing, the retailer identifies the industry leader. and then replicates the leader's prices. In using this method, the retailer assumes that the industry leader is best equipped to select appropriate price levels for its products.

Retailers often "shop" the competition to ascertain competitors' price structures. A representative from the retailer's organization visits a competitor's store to see what prices are set for the product mix. Retailing competitors, especially when done in person do not always welcome shopping the competition. It is understood that environmental scanning should be an ongoing not sporadic process, however, so many retailers see these actions as necessary.

9.8 DEMAND-ORIENTED PRICING

Under the **demand-oriented pricing** method, prices are set based on consumer demand. In this approach, retailers often raise prices based on unusual environmental changes. These changes might include unusually high customer demand *(e.g.,* for fad products), events such as natural disasters, or conflicts in other countries that affect supplies of various products such as gas or oil. In some instances, retailers raise their prices to exorbitantly high levels, a tactic called **price gouging.**

Although this tactic may appear to be a sound business practice, it is an ethical area. Customers may pay the demanded price initially, but they may harbor negative feelings toward the retailer, thus decreasing long-term business and goodwill. The three major types of demand-oriented pricing are modified breakeven, consumer market, and industrial market pricing.

MODIFIED BREAKEVEN PRICING. **Modified breakeven pricing** assumes the retailer estimates the market demand for the product and then applies it to the breakeven point. In so doing, the retailer can estimate, or forecast, sales at different price points or levels.

CONSUMER MARKET PRICING. When using a **consumer market approach** to pricing, the retailer generates data about prices based on controlled store experimentation. Many techniques can be applied here, but the general idea is that consumers enter the store and are allowed to make product purchases. The prices on the various products are changed, and the retail researcher tracks the price points that are most popular with the consumers.The retailer then implements these price points throughout its locations

INDUSTRIAL MARKET PRICING. A technique much like the consumer market approach is the industrial market approach. With this approach, the retailer sells its products to other businesses in addition to the final consumer. The retailer performs a whole selling function aimed toward other businesses.

9.9 SUMMARY

Arriving at the right price for a product or service is one of the most difficult tasks of marketing. In order to arrive at the retail price, one needs to first consider the elements that go into the making of the price. The elements to be considered are the Cost of Goods and the Merchandise Margins.

Various other factors, like the target market, store policies, competition and the economic conditions need to be taken into consideration while arriving at the price of a product. The pricing strategy adopted by a retailer may be cost-oriented pricing, demand-oriented pricing or competition oriented pricing.

The pricing strategies that may be followed include, Market Skimming, Market Penetration, Leader Pricing, Price Bundling, Multi-unit Pricing, Discount Pricing, Every day Low Pricing and Odd Pricing. Adjustments to retail prices are made by way of markdowns. Markdowns are a permanent reduction in the price and may be done as a result of slow selling or as a part of a systematic strategy.

Check Your Progress Questions

1.What are the elements of retail Price?

2. What are the components of promotional pricing?

3. What are the types of Psychological pricing?

4.What are demand oriented pricing technique?

9.10 Answer to 'Check Your Progress' Questions

1.Retail Price = Cost + markup

2.Promotional pricing includes Leader pricing and Special event pricing.

3.Psychological pricing comprises of odd/even pricing, reference pricing and Prestige pricing.

4.Demand oriented pricing techniques are Modified break even, Consumer market and industrial market pricing.

9.11 Exercise and Questions

1.Describe the elements of retail price with assumed illustration and adjustments based on the assumption.

2.What are the potential pricing objectives?

3.Discuss various methods of pricing in retail with suitable examples.

9.12 Further readings

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985

Unit 10

Structure:

10.0 Introduction
10.1 Unit Objectives
10.2 Elements of retail mix
10.3 Advertisements- Budgeting
10.4 Advertising – Methods , Pros and Cons
10.5 Sales promotion – Methods , Pros and Cons
10.6 Public relations – Methods , Pros and Cons
10.7 Personal Selling – Methods , Pros and Cons
10.8 Integrated marketing communication
10.9 Summary
10.10 Answers to 'Check your Progress' Questions
10.11 Exercise and Questions
10.12 Further Readings

10.0 Introduction

In todays competitive world, retailers strive hard to communicate their customers about their offerings and try to attract them to their stores where they can meke purchese more impulsively. The marketing tools which a retail organization use to attain its objectives is termed as the marketing mix. This chapter deals with the process of designing a marketing communication mix and various methods of communications, their advantages and disadvantages.

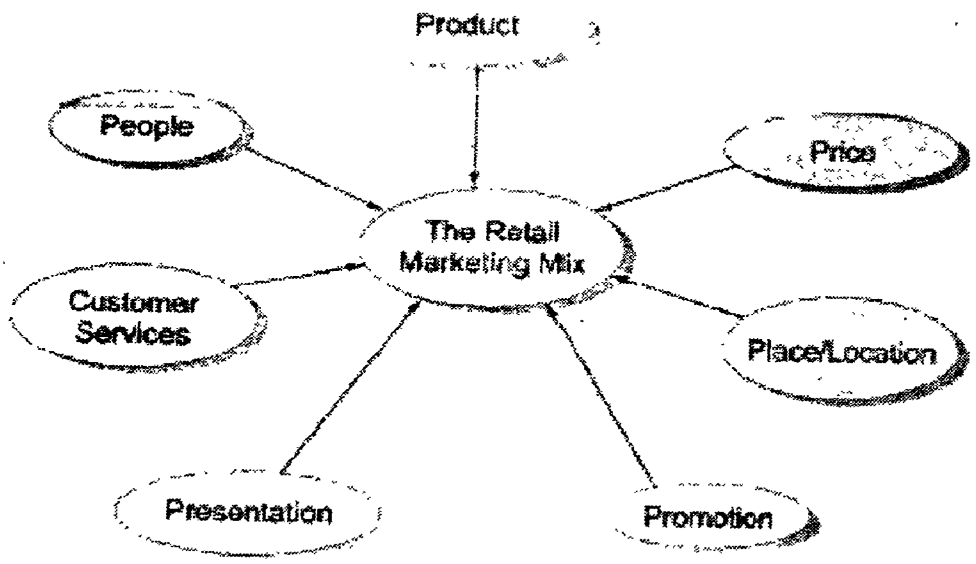
10.1Unit Objectives

- Understanding various elements of marketing mix
- Discussing objectives, methods , advantages and disadvantages of various modes of retail communication.
- Understanding Integrated Marketing Communication

10.2 Elements of Retail Marketing Mix

The main elements of the retail marketing mix are

1. the products and/or the services that the Store offers to the 'customer.
2. Create a desire to want a product.
3. To communicate the store's policy on various issues.
4. To identify the store with nationally advertised brands.
5. To reposition the store in the mind of the consumer.
6. To increase the sales of specific categories, or to generate short-term cash flows - by way of sales, bargain days, midnight madness schemes, etc.
7. To reinforce the retailer's corporate identity.



10.3 Determining the Advertising/Promotional Budget

While there is no definite formula for determining the advertising or the overall promotion budget, the following are the main methods that may be employed to determine the advertising budget

a. Percentage of ***Sales Method:*** This is perhaps the most commonly used method for determining the budget. Here, the budget is a fixed percentage of the sales. The biggest advantage of this method is that it is simple to apply and it allows the retailer to set an affordable limit on promotional activity. This method however, gives little consideration to market conditions or special advertising needs

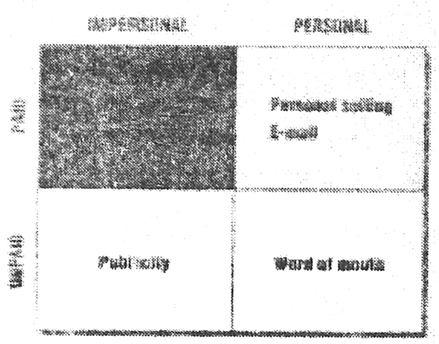
b. ***Competitive Parity Method:*** Here, the budget is based on the estimated amount spent by the competition. There is a risk that it could be based on wrong information and again, there is little consideration for market conditions or growth opportunities.

c.***Research Approach*** **or** ***the Task and Objective Method:*** The budget is determined on the basis of a study of the best forms of advertising media and the costs of each. The retailer formulates advertising goals and then defines the tasks necessary to accomplish these goals. Next the management determines the cost for each task and adds up the total to arrive at the required budget. Here, the advertising expenses are linked to the retailer's objectives and the effectiveness of some forms of advertising can be measured and compared to the costs.

d. Incremental Method:The budget is simply based on the previous expenditure

e. ***What*** **can** ***be Afforded:*** The budget allocated for advertising or for promotions, is based on the basis of the money that can be allocated by the retailer, for this purpose.
While determining which method is to be adopted, a retailer needs to take into consideration, the market that the firm is operating in, its current market position and how important advertising is in that market.

Determining the Message and the Communication Platform



10.4 Advertisements

For advertising, a retailer may use anyone, or a combination of the rollowing mediums:

Press advertisements

Posters and leaflets, brochures and booklets;

Point of purchase displays; and

Through mediums like radio, television, outdoor hoardings and the internet.

The advertising message is often a major factor affecting the success or failure of the advertising campaign. To start with the retailer needs to determine what to say. This is largely dependent on the advertising objectives and the target consumer, but the appeal has to be finalized.

At this point, the retailer needs to consider who the potential customers are; their demographic, economic and psychological characteristics; how many of such customers exist and who influences their purchasing decisions and the frequency of their buying and the type of merchandise frequently purchased.

After determining what to say, the retailer needs to determine how to communicate the message.

Some platforms which may be used, are listed below:

- Stressing the unique features of the product/s sold in the store.
- Reflecting a lifestyle or a desired lifestyle, by showing people shopping in a particular environment.

- Testimonials from celebrities. A frequently used message tactic is to have a spokesperson that champions the brand, in an advertisement, rather than simply providing information. When a position of advocacy is taken by a spokesperson, in an advertisement, it is known as a testimonial. In most cases, television, film or sports personalities with whom the target customers can identify with, are used for testimonials.
- Association formats use analogies to convey the message, by creating the mood and communicating the psychological benefits by way of exciting associations.

A retailer may also use an advertorial .An advertorial is a special advertising section, designed to look like the print section in which it appears. They are so named because they have the look of the editorial content of a magazine or newspaper, but really, represent a long and involved advertisement for the brand.

The main media used for advertising are press, television, radio, cinema, posters, hoardings and direct mail. Advertising may also be done on bus shelters, buses, road dividers, kiosks, balloons, etc. The kind of media vehicle chosen by the retailer, largely depends on the reach of that particular medium, to the target audience. For example, a Food Bazaar or Big Bazaar may advertise on a bus in a city, whereas, a store like Beautiful Boulevard, may need to advertise in an up market magazine.

The changes in technology have also made an impact on the area of communications. The internet has emerged as a legitimate option for the marketers. The web offers the marketers, a new method of selecting precise markets, focusing on specific interest areas, geographic regions, etc. It also allows the tracking of how users interact with the various brands/advertisements. On-line advertising allows the marketer to advertise twenty-four hours a day, seven days a week, at the convenience of the consumer. As most retailers today have a web presence, web advertising can be integrated with other forms of advertising.

Advertising on the Internet may be in the form of banner ads--where the ads are placed on sites that contain editorial material. It allows the browser to visit the website by merely clicking on the ad. A pop up ad may also be used. This is an ad that appears when a web page is being loaded or after it has been loaded. Lastly, communication on the Internet may be by way of an e-mail message sent to the receiver. Certain websites ask permission from the users to send e-mail updates on new existing items of interest. This is called permission marketing. After the advertisement has been created, the timing and scheduling has to be finalized and then the evaluation has to be done.

10.5 Sales Promotion

A sales promotion can be defined as a paid, non-personal form of communication that offers incentives to customers for visiting a store and/or purchase merchandise during a specific period of time. Sales promotion helps a retailer by way of attracting customer traffic and enables quick results to be achieved. Depending on the type of promotion carried out, it can help increase impulse buying, generate excitement and can motivate other channel members.

However it should be remembered that too many promotions might detract from a retailer's image and the customer may end up waiting for a promotion to make the purchases. A retailer may create sales promotions targeted at consumers or at other channel members.

Sales Promotions Aimed at Consumers

A retailer may create a sales promotion aimed at the consumer, for various reasons. Some of these reasons are listed below:

- To stimulate trial purchases: This is usually done when a firm wants to attract new customers. A reduced price or a rebate may induce trial purchases.
- To encourage repeat purchases: In-package coupons, valid for the next purchase, are examples of promotions aimed at encouraging repeat purchases.
- To encourage larger purchases: Price reductions, two for the price of one, a

discount on the second purchase, etc., are examples of the same.

- To introduce a new brand/product: A sales promotion may be done to attract attention to a new product/brand or service that has been launched by the retailer and to induce trial purchases.
- To counter a competitor's strategy: Through market intelligence, if the retailer becomes aware of a competitor launching a new product or brand, he may want to counter that launch by introducing a sales promotion.

Sales promotion goals include:

- Complementing other promotion tools
- Increasing short-term sales volume.
- Maintaining customer loyalty.
- Emphasizing novelty.

Advantages and Disadvantages

The major advantages of sales promotion are that:

- It often has eye-catching appeal.
- Themes and tools can be distinctive.
- The consumer may receive something of value, such as coupons or free merchandise.
- It helps draw customer traffic and maintain loyalty to the retailer.
- Impulse purchases are increased.
- Customers can have fun, particularly with promotion tools such as contests and demonstrations.

The major disadvantages of sales promotion are that

- It may be hard to terminate certain promotions without adverse customer reactions. . The retailer's image *may* be hurt if trite promotions are used.
- Frivolous selling points may be stressed rather than the retailer's product assortment, prices, customer services, and other factors.
- Many sales promotions have only short-term effects.
- It should be used mostly as a supplement to other promotional forms.

Common Retail Promotions

Coupons: A coupon gives the buyer a reduction in the price of specific merchandise or products at the time it is redeemed. Coupons may be delivered through newspapers, magazines, post, or in the products. An example of this is Domino's Pizza, which regularly sends coupons to customers through newspapers. These coupons offer a certain amount of discount on placing an order, during a specified time frame.

Contests: A contest requires the consumers to compete and the prizes are based on skill. In the case of sweepstakes, the customer only needs to enter in his name and the winner is determined by chance. Many retailers allow customers to enter into competitions on the basis of the amount for which they have made purchases.

Demonstrations: Demonstrations are used to show the customers, the performance capabilities of the products. Videos may also be used to aid the demonstration and highlight the uses of the products. Company executives demonstrating the use of home appliances in a supermarket, is a good example of such promotions.

Product/Brand Promotions and Schemes: This is a straightforward scheme in which the consumer either gets monetary discount on the purchase of a particular products or gets two products of the same type, for the price of one - the "buy one get one free" scheme is an example of the same.

Samples: Getting consumers to simply try a brand can have an effect on decision-making. Sampling provides the consumer an opportunity to use the product, at no cost. Various techniques may be adopted for sampling and this may take the form of in-store sampling where the in-store staff hands out the samples door-to-door sampling, or sampling through mail or with newspapers and magazines.

Frequent shopper programmes: Most retailers have frequent shopper programmes, where a member accumulates points for every purchase. Members often get invitations to events sponsored by the retailer or associates

Many retailers create a retail calendar that lists out the promotion/event schedule, for various months. This not only helps in planning, but also helps detail out responsibilities and expenses that are going to arise

Sales Promotions Directed at Trade or Channel Members

A retailer may also use sales promotions to interact directly with the members of the trade. This may be done by way of taking part in trade fairs, exhibitions and conferences. Trade fairs and exhibitions are gradually becoming popular in India. For the manufacturer, it is an opportunity to showcase his products and services and to interact with the buyers. In India, the India International Garment Fair, India International Leather Fair, Textile Machinery Exposition, Leather Goods Fair, etc., organized by the government and various commercial bodies, are examples of the same.

The basic idea of a sales promotion is to attract attention to the brand or to the retail store. Care should be taken to ensure that the coordination between advertising and sales promotions is done properly.

10.6 Public Relations and Publicity

Public relations is a marketing communications function, which aims at fostering goodwill. An important component of public relations is publicity. By way of public relations, the retail organization strives to create and sustain a favorable image in the minds of its consumers, shareholders, suppliers, and the public at large. The job of public relations is usually handled by an outside public relations firm and may be undertaken to promote goodwill for the organization, to promote a particular product or service or to counteract negative publicity.

Objectives

Public relations seeks to accomplish one or more of these goals:

- Increase awareness of the retailer and its strategy mix.
- Maintain or improve the company image.
- Show the retailer as a contributor to the community's quality of life.
- Demonstrate innovative Products
- Present a favorable message in a highly believable manner.
- Minimize total promotion costs.

Advantages and Disadvantages

The major advantages of public relations are that:

- An image can be presented or enhanced.
- A more credible source presents the message (such as a good restaurant review).
- There are no costs for message time or space.
- A mass audience is addressed.
- Carryover effects are possible (if a store is perceived as community-oriented, its value positioning is more apt to be perceived favorably).
- People pay more attention to news stories than to clearly identified ads.

The major disadvantages of public relations are that:

- Some retailers do not believe in spending any funds on image-related communication.
- There is little retailer control over a publicity message and its timing, placement, and coverage by a given medium.
- It may be more suitable for short-run, rather than long-run, planning.
- Although there are no media costs for publicity, there are costs for a public relation planning activities, and the activities themselves (such as store opening)

An organization may conduct its public relations effort by way of press releases, feature stories, and company newsletters or through interviews with the press or press conferences. Publicity is a non paid form of media coverage. In today's world, it is rarely free and a fair amount of skill has to be exercised by the organization to ensure that the right media coverage is achieved. Examples of events in retail, which may merit publicity, are:

Store Openings
Store renovations
Designer Associations
New product ranges and launches
Awards received by the retailer; and
Fashion shows and sponsored events

In order to gain positive publicity, considerable amount of effort has to be put into creating the press kit, and holding the press conference. The event or the promotion or the features of the product have to be discussed with the members of the press. The press may need a history of the organization, which needs to be researched and written well Considerable effort also needs to be put into arranging the photo sessions that may be required.

10.7 Personal selling

Personal selling may occur within the environs of the retail store-where personal selling deals with the sales person satisfying the needs of the consumers. It may also occur outside the retail store where orders are taken from customers through the telephone, Internet or mail, which are then serviced.

Objectives

The goals of personal selling are to:

- Persuade customers to buy (since they often enter a store after seeing an ad).
- Stimulate sales of impulse items or products related to customers' basic purchases.
- Complete customer transactions.
- Feed back information to company decision makers.
- Provide proper levels of customer service.
- Improve and maintain customer satisfaction.
- Create awareness of items also marketed through the Web, mail, an telemarketing.

Advantages and Disadvantages

The advantages of selling relate to its personal nature:

- A salesperson can adapt a message to the needs of the individual customer.
- A salesperson can be flexible in offering ways to address customer needs.
- The attention span of the customer is higher than with advertising.
- There is less waste; most people who walk into a store are potential customers
- Customers respond more often to personal selling than to ads.
- Immediate feedback is provided.

The major disadvantages of personal selling are that:

- Only a limited number of customers can be handled at a given time.
- The costs of interacting with each customer can be high.
- Customers are not initially lured into a store through personal selling.
- Self-service may be discouraged.
- Some customers may view salespeople as unhelpful and as too aggressive

Personal selling is precise. It is aimed at a specific individuals. Developing a strong sales force is hence, an expensive proposition, as the sales person has to be trained on the various aspects of communication, including the understanding of the body language of the customer. He also needs to be knowledgeable about the features of the products and services offered by the retailer.

POP

The Dictionary of Retailing defines Point-of-Purchase communication as the promotional signs and interior displays, often located at the point of sale or alongside displays of merchandise. Point-of purchase (POP) displays have become integral to retail, today. They help reinforce the store/product image, enhance retail sales through floor communication and provide information to the customer.

The basic function of POP in a retail store, is to induce sales. It works with advertising and sales promotions, to reinforce the messages being communicated. The communication materials for this purpose, in a retail store, include posters, danglers, flyers, glow signs, translates, banners, etc.

A research done by the Point-of-Purchase Advertising Institute (POPAI), revealed that" 70 per cent of all purchasing decisions are made in-stores. In case of mass merchandisers, 74 per cent of brand decisions are made in-store. At supermarkets, 70 per cent of brand decisions are made in-store. This is an evidence of the importance of POP. While these figures are a reflection of the American market, with the rise of self-service formats in India, the importance of POP is bound to increase.

The role of POP changes significantly with the type of product being sold and the customer's involvement in the purchase. Different types of POP material would be relevant in different types of stores and environments. For example, the kind of POP material that would be used in the women's wear section of a department store, would probably emphasize the style, fashion, quality and the price. Sometimes, special offers that may be on in the store, may also be emphasized.

On the other hand, in the case of a supermarket, POP may be used to indicate the prices, the location of the products and any special or bargain offers that may be on offer, in the store. POP in a store selling consumer durables and electronics, may lay stress on the features of the product, the warranties and guarantees and the after-sales-services provided by the outlet.

10.8 Integrated Marketing Communication (IMC)

In the early 90s, the concept of mass advertising started to give way to target market advertising. Ways of making communication more effective for the target audience were needed. There was a need for synergy between the messages being sent out to the audience. This need gave rise to the concept of Integrated Marketing Communications (lMC).IMC is a concept that is designed to make all the aspects of marketing communication, such as advertising, sales promotion, public relarions and direct marketing, work together as a unified force, rather than permitting each to work in isolation.

The American Association of Advertising Agencies defines integrated marketing communications as "the concept of marketing communication planning that recognizes the added value of a comprehensive plan that evaluates the strategic roles of a variety of communication disciplines (general advertising, direct response, sales promotion, and public relations) and combines these disciplines to provide clarity, consistency, and maximum communication impact."

The power to influence the customer has now shifted to the retailer. In a highly competitive world, the retailer faces a knowledgeable customer, and increased advertising clutter. The rise of the Internet has created a new medium for advertising and communication for the retailer. Technology is a key enabled in retail. Use of technology enables the retailer to assess the audience through database technology. Faced with increasing costs and pressure on margins, an integrated approach towards marketing and communication is necessary for the retailer.

10.9 Summary

The component of retail marketing mix is Product, price, Place, promotion, presentation, People and service. Various methods of retail communication involved are Advertising, Sales promotion, Public relations and Personal selling. As the power to influence the customers vests in the hands of the retailer nowadays, they can effectively influence them using effective communication strategies which will definitely pay back in volumes to the retailer.

Check Your Progress Questions

1.What are the elements of retail marketing mix?
2. What are the methods of sales promotion?
3. What are the methods of retail communication?

10.10 Answers to 'Check Your Progress' Questions?

1.The component of retail marketing mix is Product, price, Place, promotion, presentation, People and service.
2.. Common sales promotion methods are Contests, Coupons, Demonstrations, Product / Brand promotion and schemes, Samples and Frequent shopper programs.
3. Various methods of retail communication involved are Advertising, Sales promotion, Public relations and Personal selling.

10.11 Exercise and Questions

1.Design a retail communication mix for a Grocery Outlet.

2. What are the steps involved in budgeting retail communication?

3. Discus the p os and cons of various methods of retail communication?

10.12 Further Readings

1.Retail Management- Michael Levy and Barton A.Weitz, Tata McGraw Hill, 5th Edition 2004.

2.Retail Management- ICFAI Center for management Research publications.

3.Merchandise buying and management-John Donnellan, Fairchild publications.

4.Retail Merchandising: Principles and Applications- Ralph.D.Shipp Houghton Miffin College Division, 2th 1985